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PART I

FOREIGN AND INTERNATIONAL



## THE AIMS AND METHODS OF AMERICAN POLICY IN ASIA\*

*R. N. Rosecrance*

FROM the spring of 1951 until the spring of 1956 it was the official policy of the United States to create in Asia a fully comprehensive regional defense grouping to check the military and political threat of world Communism. Recently, however, Administration statements have indicated that change is in the air. Since the President's speech of April 21, United States' policy has veered toward increasing acceptance of Asian neutrality; if this new attitude is fully developed and implemented, it will mean the inauguration of a new American approach to Asia.

If the United States is in the process of constructing a new policy in Asia, it may, perhaps, be time to take a backward look at the old policy. Old policies are sometimes good teachers, and failure sometimes a better pedagogical device than success. Was it really necessary to abandon the policy of supporting a comprehensive regional alliance against Communism in Asia, or could that policy have been reconditioned and returned to service? If its deterioration was beyond repair, what were the causes of its decay, and how can a new policy avoid the strains of operation which contributed to the early demise of its predecessor?

In this article I shall endeavor to give some tentative answers to these questions. In particular, I shall argue that the failure of the policy of the anti-Communist military alliance is absolute and that a new policy will have to come to grips with the major cause of past failure: Asian unconcern about the balance of power.

\* This essay was essentially completed before the Suez crisis raised a new barrier between the Western nations and the new nationalist Powers. This issue will doubtlessly make more difficult a growing cooperation of these two groups of nations. In particular, it poses for the United States the disagreeable choice between alienation of traditional allies and an improvement of relations with the new nationalist world. The Suez problem does not change the essential variables of the Asian situation, however; nor does it alter the necessity of good relations between the United States and independent Asia. It merely makes imperative the policy of moderation, conciliation and compromise in this dispute which we have reason to believe the American Secretary of State has consistently pursued.

## THE FAILURE OF PAST POLICY

The policy of building a comprehensive military alliance in Asia to deter Soviet expansion was based on two assumptions: that the essential problems of American policy in Asia and Europe are the same and, significantly, that the two problems can be solved by the same techniques. The first assumption is not implausible, for Europe and Asia have witnessed almost identical manifestations of Soviet hostility. Soviet intransigence in the negotiations for the conclusion of the satellite and Italian peace treaties paralleled her obstinacy in regard to the final settlement with Japan. The creation of a military bulwark in East Europe was the analogue of the militarization of North Korea and the Vietminh Republic. The coup in Czechoslovakia was the symmetrical counterpart of the absorption of Tibet and the Korean aggression.

But the reactions of Asia and Europe to the military threat of world Communism have been very different. While Western Europe and the United States rapidly constructed a defensive military bastion to deter Communist encroachment, the nations of the Pacific and Asia never collectively recognized the necessity for forming a comprehensive regional alliance against Communism. While this is in part because the Pacific nations committed to the West have differences among themselves,<sup>1</sup> the major barrier to the creation of a Pacific pact fully analogous to the North Atlantic Treaty is the cleavage between the West and the neutralist Powers in Asia. Though the first assumption of past American policy is valid, therefore, the second is false. Since the Asian states are not willing to allow the European solution to be applied to Asia, past Western policy in Asia has failed. I shall argue presently that foreseeable developments hold no promise of future success.

## REASONS FOR THE FAILURE

The reasons for the failure of American policy are clearly to be found in an investigation of the reluctance of the Asian neutralist Powers to join a Western-sponsored alliance. One account of that failure might be that the threat which inter-

<sup>1</sup> Friction between Japan and South Korea, Japan and Australasia, and the hesitation of the two Commonwealth countries to go to their deaths fighting for Formosa have represented an obstacle to common participation in a single defense grouping.



national Communism represented was never dramatically demonstrated in Asia. If this interpretation is correct, the United States might have been wise not to intervene in Korea or to contribute to the defense of French-held Vietnam and Nationalist Formosa. If Asia, like Europe, seeks a balance of power in its own area, the United States should have waited until one pan of the scale had been fully depressed by Communist weight before endeavoring to redress the balance. The immediate counter-moves which increments in Soviet position brought forth from the West may have caused the Communist threat in Asia to seem very much less important and the American intervention to protect Asia from Communist military movements very much more certain than either have been. The containment policy, or the policy of retaliation have, perhaps, been far too successful for the good of the Western cause in Asia.

Such an explanation of Asian reluctance to join a Western-sponsored military alliance, however, assumes that Western policies have everywhere succeeded in readjusting the Asian balance. This is manifestly not the case. While the West managed to maintain a relatively stable balance of power in Europe vis à vis the Russian Communists, it has failed to maintain a similar balance against the Chinese Communist and other Soviet minions in the Far East. Indeed, though the Communists have seemed to use comparable tactics in Europe and Asia, the results obtained by those tactics have been vastly different. The invasion of South Korea, the only example of unmixing Communist military aggression took place in Asia, not in Europe. The communization of China filled a great military vacuum and represented a large increase of strength in Asia that was not reflected by an equivalent increase in Soviet strength in Europe.

In Europe again, it was felt necessary to seize Czechoslovakia by a coup so sudden that Western intervention could not materialize, but the growth of Communist hegemony in Tibet was neither concealed nor rushed to a hasty completion before world sentiment could be allowed to form against it. The headlong victory of Communism in Indo-China in 1954 and the new centre of military power erected there presents a challenge which has no complete European analogue. The conference at

Geneva which ratified this shift in the balance probably represented, moreover, the greatest single American diplomatic defeat in the Far East since the failure of the Stimson non-recognition doctrine. The conclusion to which these considerations lead is that the Communist increment of power has been far greater in Asia than in Europe since 1945, and this fact suggests that if the Asian states had been as devoted to the maintenance of an Asian balance of power as the European Powers were to the preservation of a balance in their continent, the task of organizing a counter coalition against the Communists would have been easier in the East than in the West.

It would be premature, however, to accept the conclusion that Western nations are responsive to changes in the balance of power while the Asian nations operate on other principles of policy. There is a theory, currently in vogue,<sup>2</sup> which maintains that power considerations affect the course of Asian neutralist policy, but that "power" is understood in a peculiarly Asian context. According to this view, the neutrals recognize that they may lose their independence if they allow themselves to be drawn into a permanent relation with either power bloc; hence a military alliance with either side would be rejected whatever the alterations in the Far Eastern balance. While, if such an analysis were correct, Asia could not accept Britain's traditional rôle as holder of the international balance and cast its full weight alternatively upon one side or the other, it could seek to improve relations with the side losing strength.

If such an explanation were valid, one would expect to observe shifts in neutralist policy directly proportional to shifts in the power position of the major states. The record of events does not lend this theory much support, however. It suggests even that one might be able to make a case that the neutral nations formulate their policies according to perverse balance of power principles. Between 1945 and 1951 the Communist gains in Asia were immense. China was taken over and China's new rulers soon extended their control into Tibet. Even at this relatively early stage, the Vietminh was having considerable success against the French. Domestic Communist movements assumed significant proportions in

<sup>2</sup> The author is unaware of an explicit statement of this theory in the literature, but it is, nonetheless, a commonplace of colloquial academic discussion.

India, the Philippines, Burma, Malaya and Indonesia. In the last country, a Communist coup had to be suppressed in 1949. The Korean war and the Chinese intervention occurred, and though the war demonstrated the extent of the Western commitment in Asia, it also showed that one of the lesser Communist states, supported by Russia, could hold her own with the United States in a struggle of conventional arms. This latter fact was itself a great challenge to American power.

While the European nations created the Brussels Treaty in 1948, the North Atlantic Alliance in 1949 and were preparing the military forces to pose a counter-weight to Communist advances that were minor in comparison, the neutralist nations responded to the major Communist successes in Asia with increasing hostility to the West. Not only did the neutral Powers express their unwillingness to join in a comprehensive military alliance against further Communist military advances, they almost seemed more unfriendly to the United States. Indeed, in most neutralist countries, the substantial capital of prestige which America held at the end of the war had been largely dissipated by 1951. Nor was neutralist friendship for the West more manifest after the Korean aggression.<sup>3</sup> Remarkably enough, despite the favorable power change which that invasion at first represented for the Communists and the hostile and aggressive intent which it clearly evinced, India and the other states, after an initial period of cooperation, were not more inclined to come to an agreement with the West. Soon after the original invasion, in fact, Indian opinion was castigating the West for its unsolicited intervention in Asian affairs. The implication seemed to be that India would have preferred the victory of the aggressors in Korea to an American and Western intervention in Asia to re-establish a balance of force. As a result, the first years of the Korean episode saw a worsening of Indian relations with the United States which probably reached a nadir in the summer of 1951 when India rejected the Western proposals for peace with Japan.<sup>4</sup>

<sup>3</sup> It is, perhaps, significant to note that while the Korean War did not perceptibly increase Asia's fears of Soviet aggression, it was a great stimulus to European anxieties in that regard. It led, for example, to the formulation of the European Defence Community plan and indirectly to the Paris Agreements of 1954.

<sup>4</sup> It is of parenthetical significance that the reason for India's abstention on the Japanese Peace Treaty was that she felt it treated Japan too harshly, not that it permitted the resurgence of the Japanese "menace."

Recent years have seen no reversal of the hostility of the neutral nations toward the West. The principal Communist military gain since 1951 occurred in Indo-China, where the victory at Dienbienphu was transformed through the Geneva conference mechanism into a French capitulation in all of North Vietnam. This added increment to Communist strength did not deter the Asian states from decrying the Western belated and hesitating attempts to conclude a peace that would halt further Communist military advances. The South-East Asia Treaty Organization, the most ambitious attempt of the West to redress the balance of power in Asia, has received continued condemnation from the neutral nations.

Paradoxically, the conclusion to which one is drawn is that instead of leaning toward the Western cause when the Soviet military and political advance was at its height, Asia maintained friendly relations with the Russians. It almost seems that if any Asian balancing operation was in progress, it was of a perverse nature; it operated to improve the Communist position, not to worsen it. Though no nations have lost more power in Asia in the last eleven years than the Western Powers, and though no nations have gained more power in that same area than the Communists, neutralist Asia is probably closer to the Soviet Union and Communist China today than at any time in its history. Traditional balance of power analyses are inadequate to explain this fact. Not only is it true, therefore, that Asia does not balance on British principles, it does not seem to chart its course in accordance with special neutralist balance of power premises. And if this is true, while Western nations may be sensitive to variations in the balance of power, the Asian nations seem to act on altogether different principles.

We shall, therefore, have to turn elsewhere for an explanation of the principles of neutralist foreign policy. To state or to explain these principles completely would be too great a burden on the present fragmentary knowledge we have about the newly independent nations of Asia. But it may not be proceeding too far to suggest one or two attitudes which affect the foreign policy of these nations. The most obvious tenet which conditions Asian foreign policy would seem to be the insistence upon freeing Asia from Western domination. This requirement

may often be antagonistic to balance of power conceptions because it calls for the recession of Western strength in many areas without any corresponding weakening of the Soviet or compensation to the Western position elsewhere. It follows that the test which Western countries have employed to determine a threat to the balance of power is not necessarily viewed as a danger signal in Asia; it may, indeed, be considered to evince an exemplary improvement in international relations. While aggressive behavior and actual aggression have in recent years been regarded in the West as indications of an attempt to upset the balance of power, aggressive behavior directed against the metropolitan Powers is not condemned, but welcomed in Asia. And the dilatoriness and intransigence which the West seems universally to identify with uncooperative international behavior is, in the East, a legitimate weapon in the armory of the nationalists.

The reaction in Asia against Western domination and influence and the very recent emergence of Asia into world affairs give rise to other Asian attitudes toward foreign policy. In some degree the Asian entrance into world politics is similar to the beginnings of American diplomacy one hundred and fifty years ago. Some Asian states regard the contest between the United States and the Soviet Union in much the same fashion in which the United States at one time viewed European squabbles. In this light, the bipolar struggle may seem to be merely an amoral power conflict. And this is not strange. For now that Asia has thrown off the Western bonds which have pinioned it for almost half a millennium, it needs to believe that some aspects of Western life and policies are inferior to its own, for if it cannot condemn some Western habits of action, it cannot justify having revolted from them. Thus, Asia believes that European power conflicts are somehow less important or less real than the antagonism between colonial Powers and the rising nationalist movements of Asia. They are less real because the issues between Communism and the West are morally suspect on both sides; they are less important because they do not always relate to pressing Asian issues. At the extreme one might even make a case that Asia is "neutral" in the traditional sense in that the outcome of the current conflict between Com-

munism and the West is thought to be irrelevant to her own international concerns.<sup>8</sup>

But if it is true that a part of neutralist foreign policy reflects a feeling of moral superiority and a belief that Asia has a unique contribution to make to the world, it is also true that Asia cannot reject all Western institutions and ideas because its nationalist revolutions have been, in no small measure, an attempt to secure for the East the tangible benefits of Western civilization. The results of these two conflicting attitudes is a curious contrariety of responses to the West. On the one hand Western technology holds the material promise which Asia strives to realize, and on the other Asia must justify her revolution by criticizing Western materialism. Because she is only too aware of the superiorities of Western life, she seeks always to be told of her own unique contributions. And those nations which take the trouble to commend her will find great recompense for the effort because Asia is still, like the United States of 1800, insecure and anxious in the realm of international relations. In a situation of suspicion of inferiority, Asia conducts a foreign policy which is conditioned by standards of personal morality that have no rôle in the foreign policies of states that have been long accustomed to foreign relations.

If these are essential elements of the Asian attitude toward world affairs, it may be possible to explain why American policy in Asia has failed and to predict whether its past policy will be more successful in Asia in the future. One conclusion which this description of neutralist attitudes enables us to draw is that Communist aggrandizement of power has been approved by the neutral nations in many situations because it has been clothed in nationalist garb. This fact, in great part, accounts for the neutralist willingness to permit a vast Communist assault on the balance of power in Asia. The salient advances of Communist strength in Asia, China, and Indo-China have been made in the guise of nationalism. The civil war in China, thus, did not destroy the balance of power in Asia, it represented the salutary destruction of Western control in China. The military operations in Indo-China did not lend a further weight to the already ponderous balance-pan

<sup>8</sup> This is obviously a conclusion which could not be drawn from any balance of power analysis of neutralist foreign policy.



of Communist power, it merely succeeded in wresting control of a part of Indo-China from the French.

Other incursions on the Asian balance are similarly justified. The Chinese absorption of Tibet may be regarded as the realization of an historic nationalist claim. The Chinese desire to reacquire Taiwan was based on the Cairo decisions of the Big Three, and the seizure of the island by mainland forces might be viewed as a police action to bring state relations into harmony with the express intention of the wartime allies, and even more important, it would secure for China a deeply-felt nationalist claim. Harder for the Asian neutralists to rationalize in terms of their preconceptions was the Communist invasion of South Korea. India originally favored United Nations action to stem the tide of the aggression there; yet, when the United States led a Western coalition into the fray India's old reaction against Western intervention in Asia proved too strong, and she dissociated herself from the U. N. police action.

This aversion to Western dominion is more significant than it may seem on the surface. For it means something that has not always been explicitly recognized: the Western Powers labor under an initial handicap in Asia which does not always hamper their Communist colleagues. To the extent the Communists are able to exploit their traditional anti-imperialist attitude in Asia, they may have a substantial initial advantage in the race for Asian support.

The Communists have, moreover, been able to turn this initial advantage to their own purposes. Messrs. Bulganin and Khrushchev on their recent Asian tour not only trumpeted the common Asian and Soviet anti-imperialist doctrines (the British were, for example, according to the Soviet metaphor "on the Burmese neck"), but they played skillfully upon the Asian susceptibilities to flattering advances from the established nations. The prolonged stay of the Soviet leaders in the rising Asian countries demonstrated an appreciation of the value of good relations with Asia that constituted a precedent for all the Great Powers. No American statesman had, to that time, expressed a similar willingness to conciliate the neutralist feeling in Asia. And the sudden trip by Secretary of State Dulles to repair the ramparts of freedom in Asia was an anti-climax to an essentially Soviet drama.

Fully as important as the anti-Western attitude which the Communists share with the underdeveloped countries is the justification and rationalization which Communist ideology gives to the neutralist efforts to find a secure place in the international world. The Western Powers have no true ideology in the Marxian sense because their goals, aspirations and past policies needed no justification in theoretical terms. The West has the asset that no Communist country or rising nationalist Power can claim: it has succeeded. It therefore, has had no need to rationalize its past dominance or its present relative supremacy. The neutral Powers, however, need a framework in which to fit their national aspirations, and they, as noted previously, need a way of justifying their revolt from Western control. The Communist doctrine provides a ready-made justification for past national efforts to cast off Western "oppression," and it also charts the course of growth to equality with the Great Powers. The Russian example of progress toward "socialism" and the development which resulted from the application of collectivist theories to the Russian economic system are the tangible benefits of the political adoption of Marxism. These benefits weigh heavily indeed in Asian calculations.

#### CONTINUED FAILURE OF AMERICAN POLICY

When all of these factors are appraised, the outlook for the success of past United States' policy in Asia is quite bleak. If changes in the balance of power in Asia do not worry the Asian neutralists, if the Communists succeed in disguising their aims in nationalistic phraseology, if the Russians continue to vent their campaigns of friendliness and if the Marxian ideology continues to retain its attraction in Asia, it is likely that the West will never be able to mobilize an all-Asian alliance against Communism. It would be futile, for example, for the United States to endeavor to produce a reaction against Communism in neutralist circles by allowing further Communist encroachments on the Asian balance. If the United States were to withdraw its protection of Formosa in the hope that an assault from the mainland on that island would once-and-for-all demonstrate hostile Communist intent throughout Asia, it would be



acting on a mistaken apprehension.<sup>6</sup> For India, the most influential of the "undecided" nations would not regard a Communist military campaign against the last bastion of Chiang Kai-shek as an indication of Communist hostility.

The representation of the Communist government of China in the United Nations would similarly fail to end the neutralist unwillingness to conclude a military alliance against Communism. It would, doubtless, occasion a more favorable reception for America in Asia. But it would, in Asian eyes, evidence Western willingness to agree with the long-reiterated neutralist view that Communism is not the threat that America has always declared it to be. And this particular difficulty attends any new policy that the West might formulate to implement its past aim of creating a comprehensive military alliance in Asia. For the only way in which the West can today improve its reception in neutralist Asia is by approving and accepting the neutralist course of policy. And this would involve admitting that the Western policy premise was in the first instance false. If Communism is not a military menace, then there can be no reason for creating a comprehensive military alliance against it.

All the preceding arguments lead to the conclusion not only that past Western policy in Asia has failed but that other Western efforts to implement the policy of creating an all-embracing military alliance will also fail. The method used to contain Communism in Europe simply will not work in Asia, and there is no policy in prospect which could square the circle of Asian non-commitment. In this sense the failure of American and Western policy in Asia is the symmetrical counterpart of its success in Europe.

#### THE SIGNIFICANCE OF FAILURE

Having accounted in part for the failure of past Western policy in Asia, we must now try to assess its significance. If it were completely certain that the premise on which that policy was formulated is valid, Western policy failures would be of great import. But there are some grounds for thinking that the

<sup>6</sup> This does not necessarily suggest that some satisfactory settlement of the problem of Formosa and the offshore islands might not be desirable from another point of view.

West's assumption that Communism presents a military threat in Asia, if valid in the past, may not be so in the future. There are, for example, some avenues of military advance which the Communists seem to have left unexplored. Until the Bandung Conference of April, 1955, for example, there was a remarkable parallel in the situation then prevailing in Asia and that existing in Hitlerian Europe after 1933 which provided ample rationalization for Communist expansion. The neutralist conciliation of expansion seems analogous to the British and French appeasement of Hitler of a generation ago. Communist China, like Hitler's Germany, has used the language of liberal nationalism and espoused self-determination for oppressed minorities. The Chinese residing throughout South East Asia are recent representations of the German population outside the Reich in Poland, Czechoslovakia and Austria. As Hitler called for the loyalty of the Germans in neighboring countries in order to justify German intervention to halt manifest "oppressions" and to render acceptable the *Gleichschaltung* of the states which permitted these "oppressions" to exist, so until recently, the Chinese Communists called for the loyalty of the overseas Chinese, ostensibly for the purpose of creating an issue on which punitive action might be justified.

But despite the opportunities which the situation afforded them, the Chinese Communists did not seek to exploit their position; indeed, when at the Bandung Conference, they offered to negotiate with the countries concerned the ending of dual nationality for the overseas Chinese, they lost the moral counter which might have made military expansion acceptable to the neutralist states. Further, the Chinese did not attempt to seize upon the rationalization for an invasion of Burma when the time was most propitious. When the Chinese Nationalist forces entered Burma to avoid capture, the Communists might have crossed the frontier on the pretext of "hot pursuit." That the independence of Burma would have been quickly extinguished would merely have been an incidental element in the primary moral task of liquidating the enemy. And yet, the Chinese never sought to use this avenue of attack. If the Communists were disposed to advance militarily in South

East Asia, these were counters that they should not have thrown away.<sup>7</sup>

There are, of course, a number of explanations of the Chinese hesitation to press ahead with military conquest in South East Asia. One of these is that it is probably easier to justify the seizure of Formosa, and the military campaigns against the French in Indo-China than it is to explain to the neutrals a Communist invasion of Burma, Thailand or one of the Indo-Chinese states. The announced policy of Prime Minister Nehru was, moreover, not to accept the Peking régime's claim to the loyalty of the overseas Chinese. These reasons would not in themselves, however, have provided a sufficient ground for Communist Chinese hesitation because the neutrals have often acquiesced in Communist adventures that they have at one time opposed.

A more important reason for the apparent Chinese reluctance to proceed with a military conquest of territory in Asia is the probable military opposition of the United States and its associates in the area. The Korean campaign did not bring the rewards planned for it because of the unexpected American intervention; current American statements make clear that the United States is unlikely to let the Communists make any sizable military gain without some form of retaliation, whether massive or otherwise.

A further cause for the Communist hesitation to launch further military expeditions in Asia is that they do not have the proper balance of military forces to make a successful assault. The last nation which succeeded in conquering South East Asia had substantial strength in air and sea power. It was relatively well supplied in precisely those military arms in which the Chinese are presently relatively deficient. And the effort required to mount the military force required to sustain a successful attack in Asia would involve a considerable economic burden. The industrialization of China would inevitably be markedly slowed by a rearmament in sufficient depth to assure the conquest of substantial territory in South East Asia.<sup>8</sup> The factors which recently occasioned the Soviet announcement of a

<sup>7</sup> The recent Chinese occupation of disputed areas on the Burmese Frontier shows no disposition whatever to develop into a full-scale invasion.

<sup>8</sup> It should be noted, however, that the current five-year plan provides both for capital investment and substantial military expenditure. See Rostow, W. W. and

cut of over a million in military manpower also operate in China.

But aside from the military and economic burdens which such invasions would place on the Communists, there are two major reasons why it is probably not to their interest to engage in military adventures in Asia at the present time. The first is that military tactics may not be necessary. If the Communist ideological appeal, which has obvious attractions in Asia, is stepped up, there may be no necessity for undertaking military campaigns. Though the Communist victories in China and Northern Vietnam involved military factors that may have been under-assessed in the West,<sup>9</sup> their ideological components were very large. The tactics which were so successful in these two areas seem susceptible of partial application in Malaya, Indonesia, Thailand and the independent Indo-Chinese states of Laos and Cambodia. Unfortunately, there are few Westerners who will make so bold as to predict that these ideological campaigns for the allegiance of South East Asia will all fail.<sup>10</sup>

Finally, there is the reason that military aggression would be entirely out of harmony with the current Communist co-existence campaign. While the Soviet Communists announce arms reductions and seem to be moving slightly nearer the Western position on disarmament, the Chinese Communists can hardly adopt a policy of military expansion. This is all the more true because the Soviet Union is in large measure directing its re-vamped foreign policy to Asian areas. A Chinese military assault on Formosa or South East Asia, while it might not finally alienate the neutralist nations, would be so completely out of harmony with Communist tactics in that area as to nullify the force of the "new look" in Soviet foreign policy. To have that policy undermined before it has had a chance to

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associates, *The Prospects for Chinese Communist Society*, Volume II, Center for International Studies, Massachusetts Institute of Technology, Cambridge, 1954, p. 364.

<sup>9</sup> On the rôle of military factors in the Communist take-over of China see Rostow, *op. cit.*, Volume I, pp. 35-36.

<sup>10</sup> There is, fortunately, one great hindrance to a Communist ideological offensive in Asia at the present time: the co-existence campaign. The more the Soviet leaders seek to conciliate neutralist governments, the more they undermine the position of the domestic engines of revolution: the local Communist parties. In so doing, the Communist ideological appeal is suborned to a watery nationalism. From this point of view, the visit of Bulganin and Khrushchëv to India represented a great triumph for Pandit Nehru.

take shape is something that the Soviets will hardly view with equanimity.

Supporting the Russian insistence on continuity in its co-existence policies in Asia, is the Chinese recognition that co-existence techniques are by far the most successful in winning Asian respect. The first hint of Communist adoption of the new policy of conciliation came not from the Russians but from the Chinese at the Bandung Conference. The soft-spoken Chou En-lai made, according to observers, a deep impression even upon those Asian states friendly to the West. His willingness to negotiate outstanding issues seemed a fundamental change in the tenor of Chinese policy, and the success of the Chinese at Bandung<sup>11</sup> seems to have taught the Russians a lesson in co-existence techniques that they now are seeking to apply themselves in many areas of the world. Thus, if the Chinese adhere to the co-existence line and avoid further military adventures in Asia, they will not only be taking a leaf from the Russian book, they will also be implementing an established Chinese policy. And what is equally significant, they will probably be assuring thereby that the life-expectancy of the Nationalist régime in the United Nations will be substantially shortened.

#### POLICY ALTERNATIVES

If these and the previous arguments are valid, America confronts two countervailing facts in its Asian policy: the first is that its past policy has failed and that there seems no possibility of refurbishing it for future use; the second is that its failure may not be of decisive significance, because it seems probable that the Communists will not launch substantial military campaigns in Asia in the immediate future. This is *not* to say that we can be sure that the Chinese will definitely not attack the offshore islands or Formosa. No military policy can be formulated on probabilities, and the recognition of this fact will probably lead the United States to continue its defensive preparations in the Formosa Strait. At the same time, however, political policy cannot be founded on a relatively improbable military con-

<sup>11</sup> The Western press probably overstated the significance of Asian attacks upon Communism at Bandung and took too little notice of the extremely conciliatory and even ingratiating responses which Chou made to these attacks.

tingency when the current challenges in Asia are essentially political in nature.

The failure of American policy comes at an opportune time, therefore, because the new policies which the United States has in train can be formulated without exclusive reliance upon military goals. The U.S. is now able to proceed with a policy to improve relations between the Western Powers and the neutrals in Asia without insisting as the result of that improvement that the neutrals formally commit themselves to the Western cause. And if the United States will be unable to persuade the neutrals to join a military grouping with the Western Powers against the spread of Communism in Asia, it now can take some strides toward one of the paramount goals of its previous policy: a growing comity of Western and Asian states.

As the United States formulates new policies to improve its relations with Asia it will have to remember that Asian nations do not act on the same principles as the European states with which it has been most closely associated. It will have to recall that it is at an initial disadvantage in Asia and that special tact and understanding will be required if it is to cement friendships with neutral nations. A prime consideration which the United States will have to weigh fully is that the Asian states are now striving to cast aside the atmosphere of dependence in which they have been enshrouded for centuries. In particular, the United States will have to be aware that the current program of economic aid to the underdeveloped countries, though magnanimous in conception, emphasizes the old colonial relationship to a greater degree than any other American policy. If United States' aid could be administered in a fashion which calls less attention to the obvious reliance of Asian countries upon outside help, it would ease the agonizing choice which the proud Asian countries face: of accepting all necessary foreign aid or retaining all needed self-respect. A careful reading of President Sukarno's address to the Congress of last May would, in this particular respect, be instructive. Indonesia is currently willing to accept American contributions to her economic growth only if they are free of entangling commitments, and Burma has been so sensitive to the "strings" on



American aid that she has not accepted American economic support since 1953.

The present economic aid program not only suffers from weaknesses of approach, however; it seems to be founded on the debatable premise that as Communism thrives on hungry stomachs, the way to counter Asian Communism is to place primary reliance upon economic assistance. It has never been demonstrated, to this writer's knowledge, that democratic political procedures flow inexorably from economic revival and increasing standards of life.<sup>12</sup> In many countries, economic upsurge has not been the prelude to democracy but the reverse. And it is worth noting that the only two nations which embraced Communism without a full-scale military conquest by Communist armies were European and developing capitalist states.<sup>13</sup> Part of the credence of the premise of present Western policies on economic aid stems from the belief that a democracy cannot maintain itself unless its population enjoys a certain minimum standard of living. But even if this were true, it would not follow that the establishment of a sufficient living standard would lead directly to the institution of democratic political procedures.

But whether the major premise of American economic policy in Asia is valid or not, its acceptance has had an unfortunate impact upon American concerns in the area. For the inference drawn by American policy-makers has been that stress could be placed upon economic aid to the neglect of a proper political policy. Mr. Dulles proclaimed after the Asian tour by the Soviet leaders that United States' policy toward India was satisfactory because we were contributing a certain number of millions of dollars to Indian economic development each year. One might conclude that United States policy in the world at large is to consult and cooperate politically with our traditional allies and to mollify other nations by economic aid. If this conclusion is valid, America has sought to advance its political fortunes in Asia by a method almost calculated to offend. Such a policy tramps on the Asian self-respect and hints at the old colonial relation with the West: the Asians are not important

<sup>12</sup> For an excellent criticism of this assumption see Staley, Eugene, *The Future of Underdeveloped Countries*, published for the Council on Foreign Relations by Harper and Brothers, New York, 1954.

<sup>13</sup> Russia and Czechoslovakia.

enough to be fully consulted on the major decisions of American foreign policy. Thus, whatever the beneficial impact of the economic aid program in the Asian countryside, its effect in political circles has been to reinforce a conviction that Asians have long held: that the West is bent on preserving its privileged status in the world to the detriment of the new nationalist Powers. The conclusion which follows from this recognition is not only that policies of economic support of underdeveloped countries are in themselves not sufficient to bring about the improvement of relations which America seeks, but that some of their past aspects have actually hindered the fulfillment of the task which they were designed to accomplish.

If the West is to develop a policy that will overcome the difficulties of a purely economic approach, it will have to do all in its power to assuage the deep Asian resentments about the way in which Western policy is formulated. Time and again the Asians have complained that they have not been consulted in decisions of central concern to their region. But consultation alone will not be sufficient to bring about a satisfactory improvement of relations with the independent Asians; a greater willingness to reach a genuine meeting of minds will also be required. This will not mean that the United States will have to agree with the neutralists on every issue; indeed, there are some issues on which it is unlikely that America could ever agree to the neutralist position.<sup>14</sup> But possible differences should not exempt the United States from the responsibility of seeking a true political rapprochement with the Asian states. If the Communists are beginning to recognize the futility of military attempts to improve their world position, the gap between the essential interests of the United States and those of the neutral nations should be narrower than at any time in the past.

Equally as important as the obvious necessity of reaching political accords with the neutralist Powers is the need for emphasizing the great friendship and respect in which America holds the independent Asian states. The elaborate receptions and popular demonstrations which have marked the Russian attentions to the Asian leaders have had their impact on neu-

<sup>14</sup> Korea is a case in point.



tralist policy. They have served to initiate Asia into the fraternity of world Powers, and this is a recognition which the Asians will not soon forget. Each time a major nation goes out of its way to express its friendship, respect and approval of an Asian state it wins a return that is more than commensurate with the political concessions which it makes. World esteem is the token of final acceptance into the select club of nations that once represented Europe's world hegemony.

Finally, if America is to improve its position in Asia, it must appeal not only through concrete actions, but through ideas. For ideas are the vehicle in which the past, the present and the future of the underdeveloped countries are explained and rationalized. Many Western observers have commented upon the seeming inability of the West to formulate an ideological antidote to Marxism.<sup>15</sup> Whether this is inherent in Western culture need not be debated here because a hastily fabricated Western ideology to demonstrate the virtues of Western democracy is manifestly not the answer to the intellectual appeal of Marxism. The Asians have always understood the merits of Western civilization, but this grasp has not led them to develop an adjunct of Western civilization in the Far East. What the Asians do need is not an ideological justification of Western civilization but a body of concepts which explains and justifies the Asian nationalist revolution. The West may possibly make a contribution to the creation of such a framework by pointing to the relation between the principles of political democracy and national self-determination. Self-determination may be viewed as an aspect of a continuing democratic process, and in this fashion, the progress toward full democracy can be set as an aim of nationalist revolution. A Western alternative to the appeal of Marxist-Communist ideology might suggest that the rising nations of Asia have been too wont to view national self-determination as a single act and not as just one part of a process of democratic realization.

This was the fallacy of the Asian view of the situation in Indo-China. Once the French were thrown out of the north, the aims of the nationalists had been won. But the establish-

<sup>15</sup> One Western writer, when challenged to name a Western philosopher who could stand as the ideological equal of Marx, could offer humbly and tentatively, only Bertrand Russell and A. J. Ayer.

ment of an undemocratic Communist government in North Vietnam, however popular it may have been at its institution, will put an end to the process of national, democratic realization as surely as the French would have done if they had had the military strength. The lesson of Indo-China is that a nation which cannot alter its policies at the behest of national sentiment is, in one sense at least, as subservient as a territory oppressed by a colonial overlord. If such a view could be communicated and accepted throughout Asia it would help to prevent the undeniable democratic force of the idea of national self-determination from degenerating into a repressive and undemocratic political arrangement.

There are, of course, difficulties in the implementation of such a policy. It would require first that the United States take a stand in favor of national independence movements and risk offending some of the European Powers who still maintain colonial control in portions of Asia and Africa. It would not require, however, that the United States press for immediate self-government for colonies in each case, but only that it seek to foster measurable progress toward self-government and eventual transfers of sovereignty. Such a policy would also create problems with some of the nations which have risen against Western domination but have failed to institute democratic procedures internally. Again, however, America need not insist upon the immediate institution of liberal political forms, but it must suggest that this goal be kept uppermost in the minds of the national leaders and that the final victories against imperialism will only be won when there is an end to undemocratic attitudes both externally and internally.

Finally, such a policy would involve a rather complete reorientation of American attitudes toward foreign policy. Primary emphasis would have to be placed upon Asian problems in contrast to the past emphasis upon Europe. Such a policy would require the American public to consider the possibility that Communism may not pose the military threat in the future that it has represented in the past; it would also involve acceptance by Americans generally of some of the criticisms of past American foreign policy in Asia. The hostility to neutral countries which their middle course has drawn forth in American public and political circles would have to be

overcome. But there is reason to believe that such a reorientation of the American attitude toward Asia is possible, given vigorous national leadership. The heart of American nationalism, as taught in every school in the country, is the American Revolution. The links between this revolution and those currently taking place in the Asian and African countries are in the first instance obvious and can be made ever more clear. If this connection is pressed by federal policy leaders, the patriotic fervor which attends the 4th of July celebrations can be channeled to support a foreign policy which can bring the United States closer to the nations of Asia than it has been at any time since 1945.

There are, fortunately, indications that the United States has become aware of the need for adapting a policy to conform with the changed situation in Asia. President Eisenhower has evinced a desire to conciliate and accept the independent policy of the neutral nations of Asia. The invitations to President Sukarno of Indonesia and Prime Minister Nehru indicate a renewed appreciation in American foreign policy circles of the need to express our friendship for the Asian countries. It is possible that the United States may now be on the road to a creation of a policy in Asia more realistic in aim and more congenial in method than any of its past attempts to bring about a friendly and cooperative relationship between itself and the independent nations of the Far East.

#### SUMMARY

I have, in this article, endeavored to show that the attempt to apply the successful methods of European policy to Asia cannot be expected to succeed in the foreseeable future because the independent nations of Asia, unlike European Powers, do not form their policies on balance of power principles; that despite American failure to conclude a comprehensive military alliance in Asia, there are reasons to believe that the Communists will not use military means to achieve their objectives in Asia in the near future; and that the American policy, which would improve relations with the neutral nations but not gain their adherence to a military pact, must take into account their sensitivity to Western domination. Such a policy would require the recasting of the economic aid program to eliminate

aspects which emphasize Asian dependence upon Western help; it would re-emphasize American respect and friendliness for the Asian countries and further the degree of political consultation with them; finally it should involve a more favorable American attitude toward national independence movements which would at the same time express a conviction that national self-determination is but one phase of an on-going democratic process. The logical elaboration of national determination is the establishment of democracy both internally and externally.

# THE AMERICAN COMMITTEE ON DEPENDENT TERRITORIES

*John N. Plank*

## INTRODUCTION

DURING the XVIth and XVIIth centuries, Europe's thrust toward empire brought the whole of the Western Hemisphere under her domination. The succeeding two centuries saw that control largely extinguished, but even today Europe retains significant holdings in the Americas. Excluding Greenland and the Antarctic, their total area exceeds by three times that of Great Britain, or by eighteen times that of the Netherlands.<sup>1</sup>

The status of these dependent territories has been cause for recurrent concern on the part of the American republics. At the Ninth International Conference of American States, held at Bogotá in 1948, this concern led to a decision "to create an 'American Committee on Dependent Territories' to centralize the study of the problem of the existence of dependent and occupied territories, in order to find an adequate solution to that question."<sup>2</sup>

Our purpose here is to trace the fortunes and misfortunes of this American Committee on Dependent Territories (ACDT). The story is interesting, sometimes amusing. It is not, however, one of great historical importance. After the ACDT had completed its work, the situation respecting European colonies and possessions in the Hemisphere remained virtually what it had been before. "An adequate solution to that question" remained just as distant as it had earlier; indeed, from the point of view of some Latin American countries, "an adequate solution" was even farther away. The ACDT had labored valiantly, but largely in vain. It and its work faded, leaving scarcely a trace: a temporary imbalance in the budget of the Pan American Union, and a couple of bulky volumes to gather dust on the shelves of Foreign Ministries.<sup>3</sup>

<sup>1</sup> *U. S. News and World Report*, April 2, 1954, pp. 42-44.

<sup>2</sup> *Ninth International Conference of American States*, (Washington: Department of States, 1948), p. 269.

<sup>3</sup> *Informe de la Comisión Americana de Territorios Dependientes*, (La Habana: Ucar García, S.A., 1949); *Memoria de la Comisión Americana de Territorios Dependientes*, (La Habana: Editorial Lex, 1949).

But if the ACDT itself failed to accomplish anything of lasting significance, the concerns which prompted its establishment continued very much alive. How much alive they were, and are, was to be revealed at the Caracas Conference in 1954. The "colonial question" will not down.

#### FROM PANAMA TO BOGOTÁ

The meeting at Bogotá provided the Latin Americans with their first opportunity for full-scale discussion, in all its aspects, of the subject of European dependencies in the Hemisphere. Before the outbreak of World War II, indeed, the topic was hardly broached in official Inter-American circles, for the United States, which dominated the Inter-American System,<sup>4</sup> felt that colonial matters did not legitimately fall within the System's area of inquiry and activity.<sup>5</sup>

At Panama in 1939, however, the United States called upon the states of Latin America to assist it in securing hemispheric defense, and promised to consult with those states in the event that any attempt was made to transfer sovereignty over an American territory from one non-American power to another; and in 1940 the Congress of the United States adopted a Joint Resolution which reiterated the pledge made to the Latin Americans by our government at Panama. Later in 1940, at Havana, an Inter-American Meeting of Consultation of Ministers of Foreign Affairs drafted and approved two instruments designed to provide for the temporary administration and eventual independence of European possessions in the Hemisphere should their home governments—Britain, France, Denmark, and the Netherlands—be forced to cede them to members of the Axis.

These developments were important for two reasons. First, they opened for discussion by all the American states, almost for the first time, the whole question of colonialism in the Americas; and the Act and Convention of Havana were drawn by the American states acting in concert. Second, they recog-

<sup>4</sup> In 1948, the Inter-American System became the Organization of American States.

<sup>5</sup> Only once, early in the century, was the subject brought up officially, when at the Third Inter-American Conference the desirability of eliminating "penal colonies" in the Americas was discussed.

nized as a very real possibility the end of European colonies in this region.

There the matter rested until the cessation of hostilities. But when the agenda was drawn for the proposed Bogotá conference, scheduled to be held early in 1948, the topic was assigned an important place.

#### BOGOTA

Late in 1947, the government of Guatemala requested the Governing Board of the Pan American Union to include on the program of the projected Ninth International Conference of American States a proposal of Guatemala's relating to European colonies in America.<sup>6</sup> Guatemala's declaration read:

Whereas: The historical process of the emancipation of America will not be complete so long as there remain on the continent regions subject to a colonial regime;

That the colonial regime in America keeps those peoples subject to it in a state of spiritual and economic subordination that impedes their integral progress;

That the political dependence of those possessions constitutes a danger to the peace and security of the American Republics, and is the cause of deep continental preoccupation, as was pointed out in the "Act of Havana";

That colonialism, incompatible with the ideals of America and contrary to the principles proclaimed at the Inter-American Conferences, destroys the unity of the continent, which is a basic condition for the effectiveness of the Inter-American System and for guaranteeing to this hemisphere security and the benefits of peace and liberty,

The Ninth International Conference of American States Declares: That it is a just aspiration of the American Republics that colonialism in this continent be brought to an end.<sup>7</sup>

Guatemala's draft resolution was incorporated in the Program of the Ninth Conference.

It was apparent from the outset that Guatemala's position had widespread support among the other Latin American delegations. Most vociferously outspoken was the Argentine spokesman, who suggested that the Guatemalan declaration

<sup>6</sup> *Handbook for Delegates, Tenth International Conference of American States*, (Washington: Pan American Union, 1953), p. 43.

<sup>7</sup> *Memoria*, p. 8.



be broadened to include reference not only to "colonies" but also to territories "occupied" by non-American powers. This suggestion was prompted, obviously, by Argentina's contest with the British over the status of the Falklands and the Antarctic.

Argentina's specific proposal was that the Conference should declare that "colonization or *de facto* occupation be ended," and that "the legal titles that the American republics possess give rights, responsibilities, and titles against the foreign occupying nations of this continent."<sup>8</sup> This statement was too strong for Uruguay, Brazil, the Dominican Republic and Cuba; but it met with the approval of most of the other delegations.<sup>9</sup>

The United States stood aloof from the discussions during the first period of meetings, although this country's representative is known to have conferred privately with the Argentine delegate in an effort to moderate Argentina's stand.<sup>10</sup> How successful he was, no one not privy to the conversations knows; but at least Argentina did not directly attack the United States.

On April 9, 1948, the Colombian politician, Gaitán, was assassinated, an event which led to the temporary suspension of the Conference. When it reconvened, the discussion of the colonial question was transferred to the Steering Committee, which took it up on April 21 in two stormy sessions. Both Argentina and Guatemala presented lengthy appeals to justify their claims to the Falklands and to British Honduras, and to counteract the work of the British Embassy in Bogotá which had distributed to all the delegates a careful statement of the British position.<sup>11</sup> Chile, too, took advantage of this opportunity to present her title to a section of the Antarctic claimed by both Argentina and Britain.

But there was also a lively discussion of the colonial issue *per se*. Rómulo Betancourt of Venezuela took the floor, to point out that colonialism was being liquidated all over the world, and that nothing could be more incongruous than to permit its continued existence in the Americas, the world's

<sup>8</sup> *London Times*, April 10, 1948, 4:d.

<sup>9</sup> *Ibid.*, loc. cit.

<sup>10</sup> *Ibid.*, April 8, 1948, 3:c.

<sup>11</sup> *Material Informativo*, p. 43.



foremost "anti-colonial" area.<sup>12</sup> Uruguay's delegate volunteered the delightful observation that "since no American country has colonies on the continent of Europe, it is inexplicable (that) there still exist in the Americas territories under the jurisdiction and control of European nations. . . ."<sup>13</sup> Bolivia's representative submitted a substitute resolution for that of Guatemala, which would have charged the Inter-American Council of Jurists with responsibility for drafting a report "relative to the pacific means that could be employed to bring colonialism to an end in America, and to the future government of present colonies."<sup>14</sup> Mexico's Torres Bodet delivered a very thoughtful statement in which, while manifesting substantial agreement with the general position of Argentina and Guatemala, he urged discretion. He concluded: "Given the juridical diversity of the themes the Assembly has been discussing, what we desire in our declaration is the reiteration, in the most precise possible form of this postulate: America is a geographic and historic unit from which the remnants of colonialism must disappear pacifically."<sup>15</sup> El Salvador's delegate stressed the need for working closely with America's allies in Europe in resolving the problem; but he too voiced the conviction that colonialism must be eliminated. Delegates from Panama, Colombia, Peru, Costa Rica, Nicaragua and Honduras also spoke out in favor of the Guatemalan and Argentine proposals. Finally, Ecuador's representative presented a new draft resolution:

Resolved: To create a Committee to study these problems, a Committee that will be composed of one representative from each of the American States, a Committee that will be considered to be properly constituted as soon as two-thirds of its members are named. . . .<sup>16</sup>

But while support for Argentina and Guatemala was general, it was not quite unanimous. The spokesman for the Dominican Republic stated that in his view "the Conference was not competent to act *regionally* in this matter" in opposi-

<sup>12</sup> *Ibid.*, p. 44.

<sup>13</sup> *Ibid.*, p. 49.

<sup>14</sup> *Ibid.*, p. 50.

<sup>15</sup> *Ibid.*, p. 47.

<sup>16</sup> *Ibid.*, p. 56.

tion to promises made under the United Nations Charter.<sup>17</sup> The Brazilian representative expressed the position of his government: ". . . We must not try to reform, unilaterally and in haste, the articles of the Charter of San Francisco. . . . The problem of the emancipation of European colonies in America is a problem whose solution has been assured by the Charter of the United Nations. . . ." <sup>18</sup> And Secretary of State Marshall spoke for the United States:

I have listened to the able and detailed expositions on the various phases of the colonial issue, particularly the statements of the distinguished representatives of Argentina, Chile, and Guatemala. Such a mass of wealth of data have been submitted for our consideration—historical, geographical, and legal—that the impression may have been given that this committee in reaching a decision is virtually being converted into a court of law. Even if such procedure was within the jurisdiction of the committee, the great principles of law and justice, to which we all subscribe, would demand that the other party—or parties—to the disputes should be accorded a hearing. This, of course, would not be a permissible procedure for this committee.

The position of the United States can be briefly stated as follows:

1. The reaffirmation or confirmation of its devotion to the general principle that peoples of dependent territories should be helped to attain a constantly increasing measure of self-government; and

2. Its earnest desire that disputes should be settled by peaceful means available to all parties and consistent with the Charter of the United Nations.

The policy of the United States or America in regard to European colonies in the Western Hemisphere has been one of opposition to the extension of such colonies or of European political influence in this Hemisphere. This policy has been asserted on several notable, I might say historical, occasions.

With respect to the current disputes under discussion here, the Delegation of the United States would feel compelled to refrain from supporting any resolution which would appear to prejudge the conflicting claims of friendly nations. It is the hope of the United States Delegation that the interested parties will redouble their

<sup>17</sup> *Ibid.*, p. 57.

<sup>18</sup> *Ibid.*, p. 53.

efforts to seek equitable solutions based on law and justice, and in conformity with our highest inter-American traditions and ideals.<sup>19</sup>

The United States, Brazil and the Dominican Republic knew well that their words of caution were not to be heeded. Soon after General Marshall had delivered his statement, the President of the Steering Committee proposed the creation of a sub-committee, "to harmonize the diverse points of view that had been presented and to prepare a Declaration."<sup>20</sup> His proposal was approved by sixteen votes, and the sub-committee was formed, made up of members from Argentina, Brazil, Chile, Cuba, Guatemala, Mexico, Nicaragua, Colombia, Ecuador, and Venezuela.

On April 22, the sub-committee considered various proposed resolutions and declarations advanced by the delegations of Argentina, Guatemala, Ecuador and Mexico. That afternoon a draft resolution was presented to the parent Steering Committee.<sup>21</sup> Except for a few minor details, it is the resolution that appears as number XXXIII in the Final Act of the Ninth Conference. It reads as follows:

*XXXIII. Colonies and Occupied Territories in America and Creation of the American Committee on Dependent Territories.*

WHEREAS:

The historical process of the emancipation of America will not be complete so long as there remain on the continent peoples and regions subject to a colonial regime, or territories occupied by non-American countries;

The ideal that inspired the epic of the independence of America will always animate our peoples and governments, united in their moral pledge to strive by all peaceful means within their power to eliminate from the continent any status of dependency, whatever its form, political, economic or juridical;

Ever since they achieved their independence, the American States have had this common objective, which has lately been defined in precise terms at the Meetings of Consultation of Ministers of Foreign Affairs, held at Habana and at Rio de Janeiro, in Resolutions condemning colonial regimes in America and reaffirming the

<sup>19</sup> *Ninth International Conference of American States*, p. 86.

<sup>20</sup> *Material Informativo*, p. 58.

<sup>21</sup> *Ibid.*, p. 60.

right of the peoples of this continent freely to determine their own destinies;

The American States have fixed a zone of continental security to which extra-continental conflicts should not extend, as might happen in consequence of the existence on the continent of dependent territories or those occupied by non-American countries;

The principle of pacific settlement of international controversies is part of the juridical heritage of the Organization of American States, and since controversies exist between American Republics and European states over rights of sovereignty in respect to certain territories of the continent;

The *de facto* or *de jure* status of colonies, possessions and dependent or occupied territories on the American continent, or within its security zone, varies in each case, within the framework of their common status, making it necessary to carry out studies on each of them in order to find a suitable solution in each case;

It is in the spirit of the American nations to preserve and strengthen the close solidarity of all the democratic nations of both hemispheres,

#### The Ninth International Conference of American States

##### DECLARES:

That it is a just aspiration of the American Republics that colonialism and the occupation of American territories by extra-continental countries should be brought to an end; and

##### RESOLVES:

First: to create an "American Committee on Dependent Territories" to centralize the study of the problem of the existence of dependent and occupied territories in order to find an adequate solution to that question.

Second: The Committee shall be composed of one representative of each member of the Organization of American States, whose appointment shall, in each case, be communicated to the Council of the Organization before September 1, 1948, if possible. As soon as fourteen have been appointed the Council, by prior agreement with the Government of Cuba, shall convoke the Committee in order that it may be installed and perform its duties in the city of Habana.

Third: The functions of the Committee shall be the following:

a) To centralize all information on any of the above-mentioned problems referred to it by the governments and entities concerned;

b) To study the situation of the colonies, possessions and occupied territories existing in America, and the problems related to such situation, whatever their nature, with a view to seeking pacific

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means of eliminating both colonialism and the occupation of American territories by extra-continental countries;

c) The Committee shall submit a report on each of such colonies, possessions and territories to the Council of the Organization of American States which shall transmit copies to the governments of the States Members of the Organization for their information and study; these reports shall be considered at the first Meeting of Consultation of Ministers of Foreign Affairs that is held after the presentation of the reports;

d) The Committee shall draw up its own regulations.

Fourth: The creation of this Committee and the performance of its functions shall not exclude or limit the right and action of the interested States directly concerned with the problems to which this Resolution refers, to seek a solution of such problems by themselves through pacific means.<sup>22</sup>

The Resolution was voted upon in two parts. The first part, which included the "Whereas" and the "Declaration," was approved by eighteen favorable votes, with the United States, Brazil and the Dominican Republic abstaining. The second part, which included the resolution to create the Committee, was approved by seventeen favorable votes, with the United States, Brazil, the Dominican Republic and Chile abstaining. Chile's abstention in the latter case was explained by that country's delegate: "The resolution to create a Permanent Committee to study the problem of the colonies in reality has no practical utility. . . ." <sup>23</sup> He spoke truly, as events were to show.

The United States was embarrassed by the adoption of Resolution XXXIII. It was anxious to preserve a united front in the Western Hemisphere—indeed, the Conference had been called for the specific purpose of bolstering and giving more substantial organizational structure to that front. Therefore, it wanted to avoid a rupture with its Latin American neighbors on any of the important issues before the Conference for discussion. But at the same time, the United States was concerned to strengthen the defensive posture of Western Europe. Czechoslovakia had fallen to the Communists only two months before the Conference began; and the chilling winds of the Cold War were becoming increasingly dangerous. Conse-

<sup>22</sup> *Ninth International Conference of American States*, p. 269.

<sup>23</sup> *Material Informativo*, p. 62.

quently, this country wished to prevent the American States from taking any position that could disturb its European allies.

Of course, had the situation in 1948 been basically similar to the situation in 1939 and 1940, that is to say, had the European colonies been in imminent danger of passing under Soviet control, the United States undoubtedly would have adopted a different stand. Or, indeed, if Western Europe had already gone Communist, this country's attitude would have been a different one. But 1948 was for the United States a time of reaching out to Europe, not one of withdrawal from it.

As finally presented, the Resolution adopted at Bogotá was sufficiently mild to permit the United States to abstain with grace: it did not feel constrained to cast a negative vote. The Declaration stated that it was a "just aspiration" that colonialism be brought to an end, surely a moderate announcement. And the Resolution called for the creation of a Committee "to centralize the study of the problem," again, a relatively inoffensive proposal. Had Argentina had its way in the sub-committee that drafted Resolution XXXIII, however, the United States would have been forced to adopt an openly negative position, and the harmony of the "All-America Front" would have been shattered. For Argentina had urged the adoption of a nine-point declaration "repudiating the existence of . . . colonies in the hemisphere."<sup>24</sup> This would have been much too strong to permit United States acquiescence.

It is always a risky business to assign motives to nations, but in this case it is quite clear, I think, that Argentina's objective was to embarrass the United States and irritate Great Britain. Perón and his cohorts had good reason to dislike this country, for we had done everything possible, short of intervening directly, to prevent Perón's election to the presidency of Argentina in 1946. As for Great Britain, besides the Falkland Islands dispute, there was also the rankling consciousness that for several generations Argentina had been popularly regarded as "Britain's Fifth Dominion"; and much of Perón's popularity with his fellow-Argentines stemmed from his intrepid twisting of the lion's tail.

The other Latin American states that voted affirmatively on the final Resolution must have had mixed motivations.

<sup>24</sup> *London Times*, April 23, 1948, 3:d.



First, there was certainly a sincere humanitarian concern on the part of many delegations, who felt that colonialism had to be extirpated. Second, there was the feeling that the last traces of European domination of the western continents had to be eliminated. Third, there were the various claims of several states to parts of the colonial territories. Fourth, there was the developing tendency of the Latin American republics to identify themselves with other underdeveloped and aspiring states around the world, many of which had just emerged from colonial status. Finally, there was a desire to register a protest against the policies and actions of the United States. The feeling was strong in Latin America that this country was devoting far too much of its attention and resources to Europe, to the neglect of its neighbors to the south.

The deliberations at the Ninth Conference had almost no reverberations within the European colonial countries themselves. In fact, those deliberations appear to have been most studiously ignored. France's influential journal, *Le Figaro*, devoted only a few cursory paragraphs to the Conference as a whole; and while the London *Times* gave fairly complete coverage of the debates, official British comment was notably lacking. It was not until May 5, 1948, three days after the Conference had adjourned, that a British minister announced that "Britain had no intention of giving up her title to any colonies to the States of Latin America."<sup>25</sup> And this was said only in response to a casual query from the opposition bench in Parliament. It is unlikely that a more lively interest was manifested in The Hague or in Copenhagen than had been evidenced in London or in Paris.

Nor, so far as is known, was much comment forthcoming from the colonial territories. But it is significant that the elected representatives of the British Caribbean possessions, who assembled at Guadaloupe on the occasion of the Third West Indian Conference, soon after the Bogotá meeting, adopted a declaration stating that "the social, economic, political and all other affairs of the British territories are the concern solely of the peoples of these territories and their metropolitan country, and we cannot admit any right whatsoever on the part of the signatories of the Bogotá resolution to

<sup>25</sup> *Ibid.*, May 5, 1948, 6:b.

intervene between peoples of territorial units and their metropolitan government in their unfettered choice to work together for the satisfactory solution of the problems of the territories which we represent." The statement added that the ultimate goal for the people of the British West Indies was self-government within the British Commonwealth.<sup>26</sup>

#### BOGOTA TO HAVANA

The second paragraph of Resolution XXXIII reads:

The Committee shall be composed of one representative of each member of the Organization of American States, whose appointment shall, in each case, be communicated to the Council of the Organization before September 1, 1948, if possible. As soon as fourteen have been appointed the Council, by prior agreement with the Government of Cuba, shall convoke the Committee in order that it may be installed and perform its duties in the city of Havana.<sup>27</sup>

The response to this mandate was not quite overwhelming. As the September 1 deadline approached, only eight of the Latin American nations had named representatives, to wit, Argentina, Colombia, Cuba, El Salvador, Guatemala, Haiti, Mexico and Panama.<sup>28</sup> The United States, despite its abstention at Bogota, had been expected to name a delegate;<sup>29</sup> but by late August it was apparent that this country intended to shun the Committee.<sup>30</sup> Conversations regarding the creation of the North Atlantic Treaty Organization were about to begin between the United States and her European allies. It was hardly an appropriate time to undertake a study of colonialism in the hemisphere.

Nor did the other American nations rush to appoint members of the Committee. Apparently they had reached the conclusion of the Chilean delegate at Bogotá who had felt that the Committee could do no useful job. On the 27th of August it was officially announced that the first meeting of the Committee would be postponed—"until after the September meeting of the General Assembly of the United Nations at Paris."<sup>31</sup>

<sup>26</sup> Proudfoot, Mary, *Britain and the United States in the Caribbean*, (London: Faber & Faber, Limited, 1954), p. 330.

<sup>27</sup> *Ninth International Conference of American States*, p. 269.

<sup>28</sup> *New York Times*, August 24, 1948, 9:2.

<sup>29</sup> *Ibid.*, May 1, 1948, 7:4.

<sup>30</sup> *Ibid.*, August 24, 1948, 9:2.

<sup>31</sup> *Ibid.*, August 27, 1948, 17:7.



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But the Resolution had been adopted, and therefore some effort had to be made to conform to its stipulations. On September 1, therefore, the President of the Council of the Organization of American States sent out a memorandum to all the States that had thus far failed to nominate representatives, asking them to do so "at the first possible opportunity."<sup>32</sup> Even this gesture failed to elicit a satisfactory response, however, and by November 1, the number of delegates named was still one short of the necessary fourteen.<sup>33</sup> Not until the 15th of November was the fourteenth name submitted, that of the Honduran member.<sup>34</sup> Although Bolivia, Nicaragua and Uruguay had voted at Bogotá in support of the Resolution, they did not choose to appoint members of the Committee that Resolution had established.

Upon receipt of the fourteenth nomination, the President of the Council of the OAS communicated with the government of Cuba to arrange a suitable date for the installation of the Committee. March 15, 1949, was agreed upon.

On March 5, 1949, the State Department of the United States issued the following announcement:

The Government of the United States has grave doubts that the American Committee on Dependent Territories can fulfil the tasks . . . assigned to it without endangering the principles which all American states have accepted in Inter-American agreements or in the Charter of the United Nations. It is this government's view that problems resulting from the status of the territories referred to, which exist or may develop, can and should be settled under procedures which do not involve the risk of violating these principles and for which adequate provision is made in the Charter of the United Nations.

The United States, therefore, does not plan to appoint a representative to the Committee on Dependent Territories. Note has been taken, however, of the requirement of the Bogotá resolution that reports prepared by the Committee will be transmitted by the Council of the Organization of American States to the member governments for information and study. In view of the important

<sup>32</sup> *Memoria*, p. 15.

<sup>33</sup> Argentina, Colombia, Costa Rica, Cuba, Ecuador, El Salvador, Guatemala, Haiti, Mexico, Panama, Paraguay, Peru and Venezuela had named delegates by that time.

<sup>34</sup> *Memoria*, p. 15.

questions of principle involved, the United States may wish to express its views when the reports are transmitted to it.<sup>35</sup>

This decision of the United States, which was the only one reasonably to be expected in the light of all the circumstances, infuriated the governments of those Latin American countries which had appointed delegates. The Guatemalan Foreign Minister declared that the United States had set "a bad precedent in Inter-American relations." He vociferously denied that the Havana project constituted any threat to the principles accepted by the American nations in the United Nations Charter, and insisted that the meetings would only "contribute to the effectuating of the idea of liberty and independence for all peoples."<sup>36</sup> This, of course, was not an altogether candid statement of what Guatemala hoped to see the Committee accomplish. A few days later the Guatemalan Foreign Minister announced that he would like to call upon all the American nations to help his country settle its dispute with Great Britain concerning British Honduras.<sup>37</sup> It was precisely this sort of involvement that the United States wished to avoid; and the territorial claims of Guatemala to British Honduras had very little to do with "liberty and independence for all peoples."

On March 15, 1949, the Committee was installed in Havana. Representatives from only twelve of the American states were present at this opening session.<sup>38</sup> Both Venezuela and Peru, between the time of their naming delegates and the time of convocation of the Committee, had seen their liberal governments overthrown in military *golpes de estado* and the replacement of them by right-wing dictatorships. The Peruvian member arrived later to take his place on the Committee; but the Venezuelan nominee, while properly accredited by his government, never reached Havana because Cuba refused to grant recognition to the new military *junta*.<sup>39</sup>

Thus, when finally installed and prepared to undertake its serious business, the Committee actually was composed of members from only thirteen of the twenty-one American republics. This was not a hopeful beginning.

<sup>35</sup> *Department of State Bulletin*, Vol. XX, No. 506, March 13, 1949, p. 319.

<sup>36</sup> *New York Times*, March 7, 1949, 10:5.

<sup>37</sup> *London Times*, March 15, 1949, 3:d.

<sup>38</sup> *Ibid*, March 16, 1949, 3:d.

<sup>39</sup> *New York Herald Tribune*, March 15, 1949.

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### HAVANA

By the terms of the Bogotá Resolution, the Committee was assigned the following functions:

- a) To centralize all information on any of the . . . problems (relating to the existence of dependent and occupied territories) referred to it by the governments and entities concerned;
- b) To study the situation of the colonies, possessions and occupied territories existing in America, and the problems related to such situation, whatever their nature, with a view to seeking pacific means of eliminating both colonialism and the occupation of American territories by extra-continental countries;
- c) The Committee shall submit a report on each of such colonies, possessions and territories to the Council of the Organization of American States which shall transmit copies to the governments of the States Members of the Organization for their information and study. . . .<sup>40</sup>

The Committee, therefore, had a formidable assignment. If it was to achieve significant results, it would need both adequate funds and considerable outside assistance. It got neither. Let us look first at the problem of the Committee's budget.

One of the first sub-committees established by the Committee was that on Regulations and Budget. This group drew up a preliminary budget that called for a monthly allowance of \$2,980 to cover the basic expenditures of the Committee, including the provision of secretarial and clerical help, the hiring of translators, the services of press representatives, and the like. In addition, an item of \$10,000 was included to meet the expenses of any specialists who might be engaged and for paying any other extraordinary costs. Cuba, as host country, undertook to pay the costs of plenary sessions.<sup>41</sup>

This proposed budget was transmitted to the Council of the Organization of American States, which received it unenthusiastically. Particularly those countries which had not appointed members to the Committee were distressed. Nevertheless, the American Committee on Dependent Territories had been formed by vote of the Ninth Conference, and somehow or other its expenses had to be met. Therefore the ticklish question was passed off to the Finance Committee of the OAS,

<sup>40</sup> *Ninth International Conference of American States*, p. 269.

<sup>41</sup> *Memoria*, p. 112.

which a few days later submitted a report.<sup>42</sup> In it was the recommendation that the ACDT receive an allowance of \$3,000 a month for a period not to exceed four months, the necessary sums to come out of the regular budget of the Pan American Union. Of the \$10,000 that had been requested for the payment of specialists, no mention was made. The report of the Finance Committee concluded with two interesting paragraphs:

4. It would be convenient to recognize that, when an Inter-American meeting proposes the realization of a special activity or the creation of a special committee or organ, the bases for their financing should be taken into consideration at the same time.

5. It would be wise for the Finance Committee to undertake a study regarding the financing of special activities or of special Inter-American committees in which not all the Member Governments participate.<sup>43</sup>

With respect to the second matter, that of outside assistance, the ACDT fared no better. To be sure, well before the Committee was installed the Pan American Union had compiled some material that it was hoped would prove useful to the former body.<sup>44</sup> And the government of Cuba had also gone to considerable trouble to gather together a library of pertinent literature.<sup>45</sup> But there was nothing in these collections that was not easily available to the general public, and certainly nothing that could justify the creation of a special committee of delegates from the American states for their study.

Therefore, one of the first acts of the ACDT was to commission its Secretary General to contact the Secretary General of the Organization of American States to request that he address memoranda to all the American states informing them that the ACDT was now installed and would appreciate any information regarding colonies and dependent territories in the hemisphere that the states could provide.<sup>46</sup> The Secretary

<sup>42</sup> *Ibid.*, p. 127.

<sup>43</sup> *Ibid.*, p. 129.

<sup>44</sup> *Bibliografía Selecta Sobre Territorios Dependientes en América y Otros Asuntos Conexos*, (Washington: Unión Panamericana, 1949); *Material Informativo y Antecedentes Compilados por la Unión Panamericana*, (Washington: Unión Panamericana, 1949).

<sup>45</sup> *Memoria*, p. 19.

<sup>46</sup> *Ibid.*, p. 37.

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General of the OAS did this. But not a single American state responded to the plea of the ACDT!<sup>47</sup>

In addition, the Secretary General of the OAS was asked to request of the Secretary General of the United Nations that the latter: (1) send copies of all United Nations reports concerning non-self-governing territories in the hemisphere; and (2) inform all interested non-American states of the installation of the ACDT in order that these states might, if they wished, share pertinent information with the Committee. In compliance with the first request, the Secretary General of the United Nations sent copies of the publication "containing the summaries and analysis of information on Non-Self-Governing Territories . . . transmitted . . . during 1947."<sup>48</sup> These, of course, had already been secured by the government of Cuba before the Committee first met.<sup>49</sup> The United Nations report for 1948 did not reach Havana until after the Committee had disbanded.<sup>50</sup>

Respecting the second request, the Secretary General of the United Nations replied as follows:

You also ask me to notify all interested governments of the installation of the American Committee on Dependent Territories. I am forwarding a copy of your letter of 21 April to the Governments of France, the Netherlands and the United Kingdom. You will appreciate that such action on my part is for the information of these Members of the United Nations.<sup>51</sup>

It is not surprising that none of the European states sent communications to the ACDT.<sup>52</sup> Britain, indeed, specifically announced that she refused to recognize the existence of the Committee.<sup>53</sup>

One final request was directed to the Secretary General of the United Nations, and that was that he attempt to secure for the ACDT "the collaboration of the Department of Non-Self-Governing Territories of the General Secretariat of the United

<sup>47</sup> *Ibid*, p. 41.

<sup>48</sup> *Ibid*, p. 45.

<sup>49</sup> *Ibid*, p. 23.

<sup>50</sup> *Ibid*, p. 54.

<sup>51</sup> *Ibid*, p. 45.

<sup>52</sup> *Ibid*, loc. cit.

<sup>53</sup> *London Times*, March 5, 1949, 4:c.

Nations,"<sup>54</sup> that is to say, "the direct and technical cooperation" of that Department.<sup>55</sup> Such cooperation was not offered.

The American Committee on Dependent Territories began its work with insufficient American support, insufficient funds, insufficient personnel, insufficient information and insufficient expertise. Its failure was inevitable.

It had become apparent at Bogotá that a distinction had to be drawn between the question of European dependencies in the hemisphere that were the subjects of disputes as to sovereignty on the one hand, and the broader question of European colonies in the hemisphere on the other. At Havana, therefore, two subcommittees were set up, one to deal with "Occupied Territories" and the other to deal with "Colonies." Let us discuss first the work of the Sub-committee on Colonies.

Almost at once the Sub-committee was subjected to rude shocks in the form of protests from various organizations representing the colonial peoples themselves. The Caribbean Dominion Assembly challenged the right of the Committee to take up the issue;<sup>56</sup> and the British West Indian Cultural Association condemned the Committee for "assuming the right to decide the future of British peoples without even consulting them."<sup>57</sup> These communications came as an unpleasant surprise to the Committee. Apparently, the colonial peoples were not impressed by assurance of the Cuban representative that any plan devised would be "based upon respect for the will of the peoples" of these regions.<sup>58</sup>

A second group of disappointments came with the discovery that neither the United Nations nor the other American states were going to lift a finger to provide any significant help to the ACDT. Members of the Sub-committee on Colonies became increasingly aware that they were not riding the crest of a wave of popular enthusiasm.

Nevertheless, they set about with the limited materials at their disposal to prepare the reports called for by the Bogotá resolution. These materials included the 1947 United Nations reports on non-self-governing territories, *The West Indies Year*

<sup>54</sup> *Memoria*, p. 43.

<sup>55</sup> *Ibid.*, p. 46.

<sup>56</sup> *Memoria*, p. 33.

<sup>57</sup> *Newsweek*, Vol. XXXIII, No. 13, March 28, 1949, p. 44.

<sup>58</sup> *New York Times*, March 16, 1949, 14:3.

*Book for 1947-1948*, the most recent publications of the West India Royal Commission and Paul Blanshard's *Democracy and Empire in the Caribbean*.<sup>59</sup> In addition they had the use of a select bibliography prepared by the Pan American Union, but it is doubtful that all the titles listed in it were available to them at Havana.<sup>60</sup>

The sub-committee's objective was to prepare for each of the colonies a descriptive study which covers the following basic data: (1) Geographic factors; (2) History; (3) Population; (4) Culture; (5) Economic considerations; (6) Social conditions; (7) Health and public welfare; (8) Political conditions. With respect to some of the colonies, particularly the British possessions in the West Indies, it was possible to draft fairly substantial reports which treated with some thoroughness each of the categories mentioned. With respect to others, it was possible to present only the most cursory of statements. Material concerning Jamaica, for example, fills 36 pages of the published Report of the Committee,<sup>61</sup> whereas the study of the Dutch West Indies occupies only 8.<sup>62</sup> Two French dependencies, St. Pierre and Miquelon, are not discussed at all.

We are not concerned to examine here these various reports. They are, for the most part, straight-forward descriptive accounts and are valuable to the student who is interested in obtaining a superficial knowledge about some areas of the hemisphere which are relatively little known to the general public. But they assuredly cannot serve as the bases for far-reaching policy decisions on the part of the OAS, even assuming that the OAS is otherwise qualified to make such decisions respecting the colonies.

The sub-committee on colonies drafted a Resolution to conclude its work, a Resolution which was adopted unanimously by the ACDT:

1. To request those extra-continental powers which have possessions in America to cooperate in the definitive resolution of the colonial problem, a resolution that is to be based on the principles of democ-

<sup>59</sup> *Memoria*, p. 53.

<sup>60</sup> *Bibliografía Selecta sobre Territorios Dependientes en América y Otros Asuntos Conexos*, (Washington: Union Panamericana, 1949).

<sup>61</sup> *Informe*, pp. 289-325.

<sup>62</sup> *Ibid.*, pp. 111-119.



racy and liberty, to the end that their colonies and possessions may constitute themselves as independent and democratic states;

2. To take steps, in the cases of those colonies or possessions that are not yet prepared to enjoy immediate independence, to see that they are placed under Trusteeship, in accordance with the Charter of the United Nations, to the end that their population may within a reasonable time, obtain its independence.

3. The foregoing recommendations are not applicable to those occupied territories which are the objects of claims on the part of American republics, respecting which the American Committee on Dependent Territories is making special recommendations.<sup>63</sup>

This Resolution, of course, was quite extraneous to the body of the sub-committee's report. We can safely assume, I think, that it would have been adopted regardless of what the sub-committee had discovered concerning the actual situation within the colonies. But more important to notice is the fact that the Resolution does not even consider the possibility that the colonial peoples themselves might not wish to "constitute themselves as independent and democratic states." The ACDT had received its mandate from Bogotá, and at Bogotá it had been determined that colonialism had to be rooted out of the hemisphere. Therefore, apparently, what the colonial peoples felt about the matter was really of only secondary importance.

If the sub-committee on colonies was handicapped by a lack of adequate information, the sub-committee on "occupied territories" was confronted by a problem of a different order. Early in the proceedings, Guatemala and Mexico clashed head-on over the issue of British Honduras. On March 17, Mexico's ambassador to Cuba declared that "if the status of Belice (British Honduras) is changed, Mexico's territorial rights to this region must be considered."<sup>64</sup> At the same time, Guatemala insisted that the whole dependency was hers by right. Both nations, therefore, submitted to the sub-committee for its consideration elaborate statements setting forth their respective claims.<sup>65</sup>

Confronted by this conflict, the sub-committee determined to establish a "Work Group," composed of the representatives of

<sup>63</sup> *Ibid.*, p. 339.

<sup>64</sup> *New York Times*, March 18, 1949, 13:6.

<sup>65</sup> *Informe*, pp. 353-443.



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Guatemala, Mexico and Cuba, which was to draft a single proposal that would be acceptable to both parties and could be adopted as the position of the sub-committee regarding the matter. The "Work Group" succeeded in devising both an Agreement and a Recommendation concerning British Honduras. The Agreement was to the effect that all the information presented to the sub-committee by Mexico and Guatemala should be transmitted to either the first succeeding Meeting of Ministers of Foreign Affairs or the next International Conference of American States. It also included the expression of a concern that "differences between American countries regarding the territory be resolved by peaceful means."<sup>66</sup> This Agreement was approved unanimously by both the sub-committee and the full Committee meeting in plenary session.

Trouble developed regarding the Recommendation. The "Work Group" had submitted to the sub-committee a draft whose crucial paragraph provided:

That in the name of the community of ideals which exists among the free nations of the world, and in the interests of hemisphere security (the American States), exhort Great Britain to submit her controversy with Guatemala over Belice to the judgment *ex aequo et bono* of the International Court of Justice . . . with the United States of Mexico also being represented at the Court while the subject is being litigated.<sup>67</sup>

This draft was approved unanimously by the sub-committee on occupied territories. When it was submitted for approval to a plenary session of the ACDT, however, Guatemala's representative requested that it be voted on in two parts. The first part included the Recommendation down through the words, ". . . judgment *ex aequo et bono* of the International Court of Justice. . . ."<sup>68</sup> This part was approved by the ACDT. The second part, relating to the right of Mexico to be represented at the proceedings, was rejected.

The Mexican delegation was outraged and announced its intention to withdraw from the ACDT on the grounds "that the decision taken damaged the rights of Mexico."<sup>69</sup> Mexico's

<sup>66</sup> *Ibid.*, p. 449.

<sup>67</sup> *Ibid.*, p. 346.

<sup>68</sup> *Ibid.*, p. 348.

<sup>69</sup> *Ibid.*, loc. cit.

action very nearly terminated the work of the ACDT then and there. Could the Committee legitimately continue to function with accredited representation from only thirteen of the American states, one less than the required two-thirds?<sup>70</sup> A hurried series of conferences was held to determine the question, and it was decided that, since the Committee had originally been installed with the requisite number of members, its subsequent meetings could be held with no more than a bare majority of the originally appointed members present.<sup>71</sup>

But a more important question was also involved. The American Committee on Dependent Territories had been set up to present an "American" point of view regarding the continued existence of colonies in the hemisphere under the domination of "extra-continental" powers. Mexico's withdrawal fractured the limited "front" of unity that the ACDT possessed. It was therefore felt to be extremely important to placate Mexico and if possible to bring her back into the Committee. Consequently, a "Work Group of Conciliation" was established. This Group urged that the Recommendation that had caused the trouble be withdrawn, and that a substitute Recommendation, acceptable to all parties including Mexico, be substituted for it.<sup>72</sup> The ACDT accepted the "Work Group's" proposal; and the new Recommendation, while innocuous, proved to be satisfactory to Mexico, and subsequently received the Committee's unanimous approval. It read:

The American Committee on Dependent Territories resolves: to express its sympathy for every just and legitimate claim of any American nation, to 'ratify' the principles of the emancipation of America, which have been consecrated in the International Conferences of American States, and to establish as its watchword the peaceful solution of all controversies in accordance with the justice of International Law.<sup>73</sup>

Argentina's dispute with Great Britain over the Falkland Islands and the Antarctic was not discussed extensively,

<sup>70</sup> Venezuela, it will be recalled, had not officially withdrawn her nomination of a representative to the Committee, although this representative never appeared at Havana.

<sup>71</sup> *Memoria*, p. 69.

<sup>72</sup> *Ibid.*, p. 70.

<sup>73</sup> *Ibid.*, *loc. cit.*

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Argentina being content to insert in the official Report a bald statement of her position<sup>74</sup> that included no documentation.<sup>75</sup>

After the ACDT had completed its deliberations concerning "occupied territories" and had adopted its quite unsubstantial Resolution, the disputes themselves were as far from being resolved as ever. Indeed, their settlement was perhaps even more distant, for during the discussions Mexico had entered the lists as an overt contender, so that the British Honduras controversy was no longer confined to Britain and Guatemala, but had become a three-cornered affair. British Foreign Officers, while maintaining official silence regarding the meetings at Havana, must have enjoyed many a chuckle over the ludicrous performance of their Latin American rivals. Meanwhile, the bobbies continued to patrol the quiet streets of Belice, and a handful of doughty Scots continued to herd their sheep on the forbidding slopes of the Falklands. There was every likelihood that they would continue to do so for many years to come.

### PUERTO RICO AT HAVANA

The official program of the Ninth Conference which was distributed to delegates as they arrived at Bogotá made no reference to any colonies other than European ones in the hemisphere.<sup>76</sup> Indeed, the limits of discussion seemed to have been set by the approved title of the topic, "European Colonies in America," a title that had been accepted by the Council of the OAS. It appeared, therefore, that a consideration of the Puerto Rican situation was clearly outside the purview of the Conference. Nor, aside from a few allusions by Venezuela's Betancourt, was the subject of Puerto Rico mentioned during the meeting.

But Resolution XXXIII which was adopted by the Conference was more ambiguous. Its declaratory clause asserted that "it is a just aspiration of the American Republics that colonialism and the occupation of American territories by extra-continental countries should be brought to an end." In the

<sup>74</sup> *Informe*, p. 445.

<sup>75</sup> Chile not being represented on the Committee, her claims to parts of the Antarctic contested by both Argentina and Great Britain received no attention whatsoever.

<sup>76</sup> *Memoria*, p. 7.

Resolution itself, provision was made for the creation of the ACDT "to centralize the study of the problem of the existence of dependent and occupied territories . . . (and) to study the situation of the colonies, possessions and occupied territories existing in America, and the problems related to such situation, whatever their nature, with a view to seeking pacific means of eliminating both colonialism and the occupation of American territories by extra-continental countries."<sup>77</sup>

These expressions could be construed to mean that the Committee would not be overstepping the bounds of its authority in undertaking a study of Puerto Rico. It is not altogether surprising, therefore, that certain disaffected Puerto Rican groups early petitioned the ACDT to consider the case of their territory. The first of these groups was the Partido Independentista Puertorriqueño (Puerto Rican Independence Party), a respectable and fairly responsible political party which spoke for perhaps 10 per cent of Puerto Rico's electorate.<sup>78</sup> This group asked that it be permitted to send "Delegate Observers" to the meetings of the Committee at Havana and be given an opportunity to be heard there.<sup>79</sup>

The second group that requested a hearing was the extremist and fanatical Partido Nacionalista de Puerto Rico (Nationalist Party of Puerto Rico), which advocated "direct action" to drive out the "Yankee invader." This party had last nominated candidates in a territorial election in 1932, when it had captured roughly 2 per cent of the vote cast. Since then, it had become increasingly violent and irresponsible.<sup>80</sup>

But if it is not surprising that these two factions should have pleaded for representation before the Committee, it is indeed surprising, even shocking, that the ACDT should have heeded their requests. To be sure, the Committee did not authorize the two groups to send delegations to Havana, on the ground that only "States" were authorized to sit with it;<sup>81</sup> but it did

<sup>77</sup> *Ninth International Conference of American States*, p. 268.

<sup>78</sup> *New York Times*, April 16, 1949, 3:7.

<sup>79</sup> *Informe*, p. 470.

<sup>80</sup> In 1950, two of its adherents were to attempt the assassination of President Truman, and in 1954 four of its members were to indulge in a wild shooting spree from the galleries of Congress at Washington.

<sup>81</sup> *Informe*, p. 455.

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receive and study all of their communications and included them all in the Report which it submitted to the OAS.<sup>82</sup>

The decision of the Committee to consider the Puerto Rican case apparently was not taken lightly or unanimously. On March 28, the following statement was adopted:

The American Committee on Dependent Territories has studied the various petitions that have been submitted to it by interested bodies to the effect that it include in its work the study of the case of Puerto Rico and concede to the solicitants the right to nominate Observers; and after attentive consideration of the mentioned petitions, it agrees:

1. To consider itself competent to investigate the case of Puerto Rico, but taking into account the doubts which some of the delegations have manifested regarding the applicability of Resolution XXXIII to the case . . . , it has decided, without suspending its work respecting the question, to bring the subject to the attention of the Council of the Organization of American States, in order to obtain the criterion of that Organ on which are represented all Members of the American Community. . . .<sup>83</sup>

When the Committee's statement reached the Council of the OAS, it elicited a sharp response from the representative of the United States:

. . . I can say that at no time did our Delegation at Bogotá believe that Resolution XXXIII contemplated that the Committee which it established would investigate the situation in Puerto Rico. The Secretary of State of the United States made clear the position of this Government at Bogotá concerning the questions raised under the agenda item of "European Colonies in America", which gave rise to Resolution XXXIII. Had the question of Puerto Rico been discussed, I am sure the United States Delegation would also have made its position in this respect clear at the time. . . .<sup>84</sup> It is a fundamental part of the policy of my Government not to attempt to influence the Puerto Rican people in the determination of their preferences regarding their future political status. Nor do we feel any other state or group of states should attempt to exert such influence. In accordance with this policy . . . my Government

<sup>82</sup> *Ibid*, pp. 463-617.

<sup>83</sup> *Memoria*, p. 116.

<sup>84</sup> *Memoria*, p. 119.

perceives no need for the Havana Committee, however well-intentioned may be its motives, to pursue this question any further.<sup>85</sup>

Regarding the specific question raised by the ACDT communication, however, as to the Committee's own competence to decide that it could study the Puerto Rican question, the United States representative declared that he doubted whether the Council of the OAS was authorized to make that determination. Pointing out that the ACDT had been created by the Bogotá Conference as a separate agency not coming within the scope of the organs set forth in the Charter of the OAS, he suggested that the Committee was not subject to the Council. "It is my impression," he said, "that in the absence of any provision to the contrary, only the parties to such a resolution can determine its intent. For the Council to formulate a reply to the Committee would, therefore, require referral of the matter to the governments for their decision."<sup>86</sup>

The Argentine delegate felt quite otherwise. In his view, the Committee was perfectly competent to make its own decisions regarding the scope and direction of its inquiries; and the Council of the OAS was under an obligation to inform the Committee to that effect.<sup>87</sup>

After an extremely lengthy debate,<sup>88</sup> the Council approved the following statement which was transmitted to the Committee at Havana:

(The Council) agrees to: 1. Acknowledge receipt of the communication of the American Committee on Dependent Territories . . . regarding the status of Puerto Rico; 2. To transmit to the Governments, through their respective Representatives on the Council of the Organization, the statement of the American Committee on Dependent Territories and to inquire of the former whether Resolution XXXIII of Bogotá authorizes said Committee to study the situation of any American territory that is under the effective sovereignty and jurisdiction of any American State; 3. To communicate to the American Committee on Dependent Territories this agreement.<sup>89</sup>

<sup>85</sup> *Ibid.*, p. 120.

<sup>86</sup> *Ibid.*, p. 119.

<sup>87</sup> *Ibid.*, p. 137.

<sup>88</sup> *Ibid.*, pp. 135-199.

<sup>89</sup> *Informe*, p. 457.

Accordingly, copies of the ACDT communication were transmitted to all the American governments. By the time the Committee completed its work in Havana, in July, 1949, replies had been received from fourteen of the states: Mexico, Peru, Paraguay, Colombia, Honduras, Bolivia, Costa Rica, Venezuela, Cuba, Guatemala, Haiti, the Dominican Republic, El Salvador and the United States.<sup>90</sup> Of these, only those from Costa Rica, Cuba and Guatemala held that the ACDT was competent, under the terms of Resolution XXXIII, to consider the case of Puerto Rico.<sup>91</sup> Later, Panama, Brazil, Nicaragua and Ecuador also went on record. Ecuador was alone in this last group in holding that the ACDT could legitimately study the Puerto Rican situation.<sup>92</sup> It is not known whether the remaining three republics, Argentina, Chile and Uruguay, ever replied to the Council's query.

In the meantime, there was a lively reaction on the island of Puerto Rico itself. In the middle of March, 1949, La Asociación Puertorriqueña de Mujeres Estadistas (literally, Puerto Rican Association of Women Statesmen) sent a cable to the Committee at Havana:

The Association . . . desires to inform the (Committee) that the last general elections show by an overwhelming majority that Puerto Rico does not wish to cut itself off from the United States of America and that it is not in reality a colony, but rather a potential State.<sup>93</sup>

More striking than the action of the women's association was that taken by the Puerto Rican Senate on April 15, which passed unanimously and without discussion a resolution that rebuked the Havana meeting for including Puerto Rico "as a colonial problem." It censured the conference's willingness to listen to the Puerto Rican independence leaders after the Puerto Rican people had "overwhelmingly repudiated" independence in the preceding elections. It went on to say that Puerto Ricans were American citizens who enjoy "all the liberties of the most fundamental charters of humanity."<sup>94</sup>

<sup>90</sup> *Memoria*, p. 50, and *Annals of the Organization of American States*, Vol. I, No. 4, 1949, p. 389.

<sup>91</sup> *Informe*, p. 457.

<sup>92</sup> *Memoria*, pp. 249-254.

<sup>93</sup> *Informe*, p. 617.

<sup>94</sup> *New York Times*, April 16, 1949, 3:7.



The next day, the Puerto Rican House passed an identical resolution.<sup>95</sup>

Despite this show of opposition to its intervention in the case, the ACDT blithely continued to receive the reports of the dissident Puerto Rican independence groups, and to incorporate them in its own minutes and reports. Furthermore, in its Final Act, the Committee determined to transmit all the material sent it by these groups to the Council of the OAS.<sup>96</sup> And in one last show of reckless defiance, it declared, again in the Final Act, that:

. . . Given the present economic, political, and social situation of Puerto Rico, (the ACDT) favors providing Puerto Rico with the opportunity to decide expressly and freely its own destiny.<sup>97</sup>

This declaration was completely irresponsible. It was gratuitously insulting to the Puerto Rican people who in 1948 had voted to stay within the protective umbrella provided by United States suzerainty: the weak showing of the independence candidates was evidence that independence was not what the Puerto Ricans wanted. It was also insulting to President Truman, who had openly declared that the Puerto Ricans should be given full opportunity to choose any one of four types of political status, including full independence.<sup>98</sup> But the members of the American Committee on Dependent Territories, who felt with some justice that they had been crossed and balked at every turn, were in no mood to be honest or dispassionate.

On July 21, 1949, members of the Committee gathered in Havana's Academy of Sciences to sign the Final Act. It cannot have been an altogether happy occasion. The Committee's positive accomplishments had been almost nil: a compendium of useful but previously available material concerning some of the colonies in the Western Hemisphere, and a reiteration of Argentina's and Guatemala's claims to territories held by Great Britain. On the negative side, the Committee had managed to infuriate the United States and Puerto Rico, had been rent by internal dissensions and disagreements and had

<sup>95</sup> *Ibid*, loc. cit.

<sup>96</sup> *Informe*, p. 636.

<sup>97</sup> *Ibid*, p. 637.

<sup>98</sup> *Memoria*, p. 120.

revealed that the unilateral approach to the colonial question adopted by the OAS at Bogotá was fruitless.

## HAVANA TO CARACAS

Resolution XXXIII provided that the Committee was to submit reports concerning each of the "colonies, possessions and territories" to the Council of the OAS, which in turn was to transmit these reports to the various governments of the American States for information and study. The reports were then to be considered in conference by all the governments at the first succeeding Meeting of Consultation of Ministers of Foreign Affairs.<sup>99</sup>

The Committee's reports were published late in August, 1949,<sup>100</sup> and were delivered to the Council, which saw to their distribution.<sup>101</sup> Because of the outbreak of war in Korea, however, they were not considered by the next Meeting of Consultation, which convened at Washington from March 26 to April 7, 1951.

It was announced by the Program Committee of the Council of the OAS, which prepared the agenda for this meeting, that "in view of the emergency situation and of the scope and importance of the program of the Fourth Meeting of Consultation, it would be preferable to limit the topics to those that have a direct relationship to that program . . .," and that consequently the reports of the ACDT would not be discussed.<sup>102</sup>

The decision of the Fourth Meeting to bypass the reports of the ACDT was highly pleasing to the United States, which desired only to see the whole question of European dependencies in the hemisphere buried and forgotten, at least as far as the OAS was concerned. But the majority of the Latin American states, while willing to postpone discussion of the ACDT's work in the interest of presenting a united front in support of the United Nations' action in Korea, were not content to ignore the colonial issue altogether. Therefore, when Venezuela proposed that the Fourth Meeting "reaffirm the Inter-American

<sup>99</sup> *Ninth International Conference of American States*, p. 269.

<sup>100</sup> *Informe*: August 27, 1949; *Memoria*: August 31, 1949.

<sup>101</sup> *Annals of the Organization of American States*, Vol. I, No. 4, 1949, p. 352.

<sup>102</sup> *Handbook, Fourth Meeting of Consultation of Ministers of Foreign Affairs*, (Washington: Pan American Union, 1951), p. 5.

principles announced at the First and Second Meetings of Consultation" regarding colonies, the proposal was adopted by an almost unanimous vote, the United States and Brazil alone choosing to abstain.<sup>103</sup>

In part, the Declaration reads:

The Fourth Meeting . . . declares: The firm adherence of the American Republics to the following principles adopted at the First and Second Meetings of Consultation:

1. The non-recognition and non-acceptance of transfers or attempts at transferring or acquiring interest or right . . . in any territory of this Continent held by non-American States, in favor of another State outside the Continent, whatever the form used to accomplish this purpose.

2. That in case it should be necessary to apply the measures prescribed in the "Convention on the Provisional Administration of European Colonies and Possessions in the Americas", the interests of the inhabitants of those territories should be taken into account so that the gradual development of their political, economic, social and educational life may be promoted.<sup>104</sup>

Since it had been the United States which had made these proposals in the first instance, in 1939 and 1940, the United States was not in a position to object strenuously to their reiteration in 1951. But the United States could reasonably point out that the situation confronting the hemisphere in 1951 was very different from that which had confronted it in 1939 and 1940. The possibility of any transfer of colonial territories in the Western Hemisphere from one non-American power to another was far less likely in 1951 than it had been a decade earlier. And in any case the Convention of Havana was still in force in 1951, so no essential purpose was served by its re-statement.

But the Latin American countries, it is probably fair to say, had something very different in mind in pressing for the Declaration cited above. In the first place, they wanted to keep the colonial question open and before the eyes of both the American and the European public. In the second place, they wanted to register their contention that the European powers held terri-

<sup>103</sup> *Fourth Meeting of Consultation: Proceedings*, (Washington: 1951).

<sup>104</sup> *Ibid*, p. 242.

tories in the Americas only conditionally, and therefore, in a manner of speaking, on the sufferance of the American states.

Thus, although the ACDT was officially ignored in the proceedings of the Fourth Meeting of Consultation, the situation that had prompted its creation in the first place was still a matter of lively concern to the Latin Americans.

#### CARACAS

Preparations for the Tenth International Conference of American States began in 1950 with the appointment by the Council of the OAS of a Committee which was charged with drafting a preliminary agenda. This Committee was composed of representatives from Argentina, Brazil, Colombia, Cuba, the Dominican Republic, Mexico, Nicaragua, Peru, the United States, Uruguay and Venezuela. Five of the eight members on it, therefore, had also been represented on the ACDT, and if Venezuela be included, six. In view of this fact, it is significant that nowhere in the preliminary agenda is there any mention of the American Committee on Dependent Territories or its work, despite the inclusion in the program of a number of topics grouped under the heading, "Topics that have their origin in the Final Act of the Ninth International Conference of American States."<sup>105</sup> This preliminary program received the approval of the Council of the OAS on January 16, 1953.

The proposed agenda was then distributed to the various American governments for their comments. By May 30, 1953, eight governments<sup>106</sup> had responded with suggestions for changes in the program: one or more of them—we are not given to know which one or ones—urged the inclusion of consideration of the colonial question in the report of the ACDT.<sup>107</sup> Consequently, in the Draft Agenda published on July 1, provision was made for the discussion of this topic.<sup>108</sup> In the definitive Agenda, released late in 1953, it was given a prominent place, appearing as Item 2 under Chapter I.

When the Conference convened at Caracas in March, 1954, discussion of the colonial issue was at first subordinated to the

<sup>105</sup> *Annals of the Organization of American States*, Vol. V, No. 2, 1953, p. 107.

<sup>106</sup> Argentina, Ecuador, El Salvador, Haiti, the United States, Uruguay and Venezuela.

<sup>107</sup> *Annals of the Organization of American States*, Vol. V, No. 3, 1953, p. 227.

<sup>108</sup> *Ibid.*, loc. cit.

discussion of the threat of Communism to the hemisphere. But no sooner had the declaration condemning Communism been approved than the colonial question took top priority.

The debate concerning colonies and occupied territories at Caracas was strikingly similar to that which had taken place at Bogotá six years earlier, except that this time it was even more frenetic and unrestrained. Early in the proceedings, Argentina introduced a draft resolution that called upon the Conference to declare that "it is the will of the peoples of America that holdings of colonies and occupation of territories be finally ended."<sup>109</sup> This was much stronger than the 1948 resolution, which had asserted that it was no more than "a just aspiration" that colonialism "should be brought to an end." Argentina's text also provided that the Conference "proclaim the solidarity of the American republics" with their neighbors who consider the territories occupied by European countries to be rightfully theirs.<sup>110</sup> In the 1948 resolution there appeared no counterpart for this.

Even the Brazilians, who in 1948 had refused to go along with the majority of the other republics in approving Resolution XXXIII, in 1954 submitted their own draft proposal which, while softer in tone than the Argentine one, was still much stronger than that of 1948 had been. Brazil urged that the Conference "declare its firm conviction that the extra-continental countries that wield political power over portions of American territory will not delay in completing the measures comprised in the Charter of the United Nations to allow peoples affected to exercise fully their right of self-determination."<sup>111</sup> For those colonial peoples not yet fully prepared for independence, the Brazilian proposal suggested trusteeship under the supervision of the United Nations.

It is noteworthy that both the Argentine and the Brazilian resolutions bear resemblances to recommendations contained in the report of the ACDT.

Delegations from country after country arose to voice support of the Argentine and Brazilian positions: Chile, Guate-

<sup>109</sup> *New York Times*, March 16, 1954, 8:4.

<sup>110</sup> *Ibid.*, loc. cit.

<sup>111</sup> *Ibid.*, loc. cit.

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mala, Mexico, Cuba, Ecuador, the Dominican Republic, Colombia, Peru.<sup>112</sup> And a working group was appointed to effect a joining of the two draft declarations into one.

Only the United States stood aside. Explaining this country's refusal to participate in the labors of the working group, our representative stated:

Without in any way detracting from the importance of achieving genuine self-government in the dependent areas, it is our view that little or no constructive purpose would be served by detailed consideration of problems of this kind at this conference, while on the other hand such consideration might well handicap us in attainment of the objectives we all seek.<sup>113</sup>

He went on to explain that since neither the colonial powers nor their colonies were represented, it was inappropriate to discuss the matter. The only suitable forum was the United Nations.

But the Latin American nations were even less receptive to words of caution from the United States in 1954 than they had been in 1948. Despite a surface show of harmony at Caracas, tensions within the Inter-American System were beginning to show. Latin America, which had followed this country's lead in adopting the resolution condemning Communism, was not going to be restrained by the United States from condemning this country's allies.

The working group was unsuccessful in drafting a resolution that blended satisfactorily the proposals of Argentina and Brazil, and therefore each of them was voted on separately. The Argentine draft was considered first. Just before the vote was taken, however, it occurred to the Uruguayan delegate that perhaps some of the colonial peoples did not wish to be "liberated." Apparently it had not occurred to any of the other delegations. Therefore, a clause was inserted that condemned colonial rule "against the will of the peoples."<sup>114</sup> Argentina accepted the amendment with the stipulation that it was not to be held to apply to the peoples of "occupied territories."<sup>115</sup> On this basis, the final tally was taken, and

<sup>112</sup> *Ibid.*, March 17, 1954, 1:2.

<sup>113</sup> *Ibid.*, *loc. cit.*

<sup>114</sup> *Ibid.*, March 18, 1954, 1:2.

<sup>115</sup> *Ibid.*, *loc. cit.*

the Argentine resolution was accepted by a vote of nineteen to nothing. The United States abstained, and Costa Rica was not represented.<sup>116</sup> It was a smashing defeat for the United States.

Surprisingly, the Brazilian recommendation regarding trusteeship for some of the colonies was defeated, largely through accident. Four countries were absent when the vote was taken, two countries—the United States and Nicaragua—abstained, and four countries voted against the proposal. Thus Brazil could rally only ten votes in support, one less than the necessary majority. Later, however, an amended version was adopted which declared "the necessity for the extra-continental powers that have colonies in American territory not to delay in carrying out the measures comprised in the terms of the United Nations Charter to permit the peoples concerned to exercise fully their right of self-determination so that colonial rule may be finally eliminated in America."<sup>117</sup> On this, the vote was fifteen to nothing, with the United States abstaining and four other countries absent.

Nor was this the end of the story. On March 19, 1954, the Ecuadorian delegation introduced a proposal that the American Committee on Dependent Territories be continued, and that its reports be transmitted to the United Nations! This proposal the Conference accepted by a large vote. But this time the United States was not content merely to abstain. This time, for the first time, it voted against its Latin American neighbors.<sup>118</sup>

Very soon thereafter, the appropriateness of the Uruguayan amendment to the Argentine resolution was revealed, when two representatives from the Dutch colonies, one from Surinam, the other from Curacao, appeared to testify before the Conference. They stated categorically that the people for whom they spoke had no interest whatsoever in cutting their ties with the Netherlands, that the Dutch possessions enjoyed complete local autonomy except in matters of defense and foreign affairs, and that they, indeed, had more independence

<sup>116</sup> Costa Rica later subscribed to all the decisions taken at the Conference.

<sup>117</sup> *New York Times*, March 19, 1954, 9:5.

<sup>118</sup> *Ibid.*, March 20, 1954, 5:1.



than Puerto Rico. They added that they could if they wished secede at any time from the Dutch empire; but that they most emphatically did not desire to be "freed" and that they definitely were not being "governed against their will."<sup>119</sup> The reaction of the Latin American delegations to these remarks is nowhere recorded.

#### CONCLUDING REMARKS

The objective of this study has been to present as complete a picture as possible of the American Committee on Dependent Territories. An effort has been made to place the Committee in its historical context, to outline its structure and organization and to assess its operations and accomplishments. This report, of course, is not an impartial one: the author has not attempted to conceal his own prejudice against the Committee and its works. No doubt a loyal Peronista, utilizing the same materials, would have arrived at some conclusions startlingly different from those presented here. He would have stressed, for example, the "sanctimonious hypocrisy" of the United States and the "pioneering effort" of the ACDT. But one is obliged to describe and interpret the facts as he sees them; and there seems to be little that is meritorious in the Committee. These few concluding remarks will present very briefly the author's position regarding the question of colonies in the Western Hemisphere.

First, he is not at all convinced that the elimination of European control over dependencies in the hemisphere is desirable, at least not at present or at any time in the immediate future. Should the British, for example, leave the West Indies, Guiana and Honduras tomorrow, what would be the result? Almost certainly, such action would spell the end of the very promising possibility of West Indian Federation, with all that projected federation holds in terms of an economically and politically viable structure. Just as certainly, it would lead to attempts by Venezuela and Guatemala to incorporate Guiana and Honduras. Can the Venezuelans and the Guatemalans seriously expect us to believe that the East Indians of

<sup>119</sup> *Ibid*, March 22, 1954, 8:3; and *London Times*, March 23, 1954, 6:c.

Guiana or the Negroes of Honduras would be better off under their wardship than they are at present?

Or suppose that the French were to agree to abandon Martinique and Guadeloupe. No matter how benign and enlightened the trusteeship that supplanted French control, there is not the slightest possibility of these two little territories ever being able to achieve significant independence. And even if we concede, as we must, that conditions on the French islands are deplorable, can we say that the Haitian peasant enjoys better ones? One would hesitate even to suggest it.

As for the claim that it is essential that the last traces of European empire be eliminated from the hemisphere, it is time we ceased being childish. The whole Western Hemisphere, in almost every important social and cultural sense, is a creature of Europe; and what is urgently called for today is a strengthening of our ties with Europe, not a senseless fretting about imperial residues. The myth of "hemispheric isolation" must be scotched: the time has come to stop talking in noble terms of "America's high destiny," and to begin talking about the destiny of the Atlantic community, of which both Europe and the Americas are parts.

Nor, is the author much impressed when our Latin American neighbors talk about "violations" of the "sacred rights of man" in the colonies. What of these same "sacred rights" in Venezuela, in the Dominican Republic, in Colombia, in Nicaragua, in Peru? We do not for a moment wish to imply that the absence of effectively functioning democratic institutions in these Latin American countries justifies in any way their absence in some of the colonial territories. But we think that it ill becomes representatives of Pérez Jimenez, Trujillo, Rojas Pinilla, Somoza and Odría to talk righteously of violations on the part of the British, French, and Dutch.

This brings us to another issue, and that is the question of the propriety of discussing the matter of European dependencies in meetings of American states. Let us grant that in 1939 and 1940 the hemisphere was confronted by a serious situation, and that the possibility of the West Indies passing under Nazi control was a dangerous threat. Under those circumstances it was entirely legitimate to take emergency meas-

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ures. But the Resolutions adopted at Bogotá and Caracas were not determined by considerations of hemispheric security. They were, instead, politically motivated.

In the author's view it was entirely inappropriate for the Latin American republics unilaterally to adopt those Resolutions concerning territories over which they had no control and in the absence of representation either of the colonial powers or of the colonial peoples. The United Nations does provide a forum for the discussion of such colonial questions; the OAS emphatically does not.

## GROWTH PROBLEMS IN INTERNATIONAL TRADE

Ajit Sen Gupta<sup>1</sup>

### INTRODUCTION

THE broad purpose of this paper is to appraise existing international trade theory, first, in terms of its logical consistency, second, in terms of its capacity to provide fruitful policy insights regarding realistic, dynamic economic problems. Most of the controversies on policy and analyses in the field of international trade theory can be traced down to four main factors, (a) application of static equilibrium theories to essentially dynamic problems, (b) lack of proper integration of real and monetary analyses, (c) use of aggregate macro-economic analyses to what may be essentially problems originating in particular sectors of the economy and (d) the failure to relate some more or less accepted conclusions regarding dynamic consequences of growth in a closed economy to problems of international economics. Some of these methodological deficiencies of international trade theory have been pointed out by Professor Haberler in his recent *Survey of International Trade Theory*. Haberler says:

A distinction is commonly made between the 'monetary' and 'pure' (or 'equilibrium') theory of international trade. The former deals with the methods of adjustments in the balance of payments and with the determination of exchange rates. The latter abstracts from the monetary mechanism and attempts to describe the conditions of equilibrium in 'real' magnitudes. How the two types of theories are interlocked has by no means been fully explained. Similarly, in economic theory in general, the logical integration of monetary theory, macro-economic employment theory and the theory of business fluctuations on the one hand, and of price and value theory on the other continues to present us with many unsolved problems. The monetary theory of foreign trade is in part a dynamic theory. The pure theory of international trade, however, is a part of general value and price theory. Furthermore, the classical theory of 'comparative costs' and the more general version which

<sup>1</sup> The author is indebted to Professor Seymour E. Harris for valuable criticisms of the original draft of this paper. The views expressed are the author's and do not necessarily reflect those of the International Monetary Fund.

succeeded and elaborated it, are static general equilibrium theories. . . . As far as abstract theory is concerned, there exists, . . . not much more than occasional hints and programmatic pronouncements concerning the necessity of dynamizing traditional theory plus a few fumbling steps in the direction of the actual construction of dynamic models. *Economic history has more to offer than theoretical analysis for the solution of these problems.*<sup>2</sup>

The importance of these observations can hardly be exaggerated. Yet in some recent discussions on comparative costs, freely-floating exchange rates and differential rates of growth of productivity in different nations, static and dynamic, real and monetary analyses have come closer together and often an illusion is created that the integration of these elements (vitaly necessary for the prescription of monetary and other policies for the solution of international trade problems) has already been effected. It is true that immediate policies cannot wait for the formulation of an integrated theory, but policies tend to be rationalised or opposed in terms of theory; and with theory at its present stage it is no wonder that there should be so many policy-controversies in this field. This paper attempts to locate the fundamental sources of the controversy—a controversy which in different historical contexts have continued for over a century and a half in our literature—and offers some suggestions for the proper understanding and interpretation of the theory and historical practice of international trade. There is, of course, no attempt to formulate any kind of an integrated, dynamic international trade theory. We hope, however, that a broad (logically not too rigorous) picture may emerge which may stimulate thinking on more basic international trade problems.

#### COMPARATIVE COSTS: REAL AND MONETARY ANALYSES

The conclusions, broadly speaking, of most academic economists on the fields of international trade theory we are discussing are:

(1) Regarding comparative costs and the general case for free trade, the presumption is that the case for free trade based on comparative advantage is still valid, though there are some

<sup>2</sup> *A Survey of International Trade Theory*, Gottfried Haberler, pages 4 and 55. (International Finance Section, Department of Economics and Sociology, Princeton University, 1955.) (Italics ours.)

objections to the general rule. As Hicks puts it, "the positive argument for free trade is valid as ever; what has happened is that the exceptions have grown up and in the minds of many have overshadowed the positive argument. We can, I think, grant that these exceptions (many of which have long been familiar) were given too little weight in the past; but we should be wary of giving them too much weight now."<sup>3</sup> The exceptions specifically dealt with by Hicks are the external economies and diseconomies argument, the monopoly competition argument, the unemployment argument, the infant industry argument and the terms of trade argument. Hicks considers each of these exceptions separately and does not consider whether they could possibly operate together in a dynamic economy to damage substantially the logical case for free trade. He is inclined to look favorably only on the employment argument and the Listian motives for protection, particularly for under-developed countries.

(2) With tariffs justified for technological growth in relatively backward nations, the international economy *tends* to be more and more competitive rather than complementary. Tariffs and technology helped Western European nations and the U.S.A. to develop competitive rather than complementary economies and once national economies are built up by protection for competition through free trade, changes over time in relative rates of technological advance in different industries in different countries may again create a pressure for protection to avoid domestic instability and to re-create afresh the technological capacity for competition. The narrowing of the gap of comparative advantage not only reduces the gains from trade, it increases the uncertainties and instability of free trade, particularly in view of the immobility of factors of production internationally. As we shall see, most of these problems have been recognized, particularly in the writings of Williams, Robertson and Viner. All of them are convinced of the irrelevance of the classical theory of comparative costs in the present situation. Again, all of them are equally convinced that protection and exchange-controls are not *basic* solutions to the problem.

<sup>3</sup> J. R. Hicks, *Free Trade and Modern Economics*, Manchester Statistical Society, 1951.

(3) Free trade is not a complete substitute for free mobility of factors in equalizing factor-prices internationally. To quote Mead, "free trade tends to equalize factor prices only when a sufficient number of freely tradable products are simultaneously produced in a number of countries." There are six possible cases when free trade will not bring about complete factor-price equalization, in the case of complete specialization (before the marginal productivity of factors have been equated between, say, two freely trading countries), in case of different productive atmospheres, social, psychological and geographical climates, etc. (the same amount of land and labor will not produce the same amount of grapes in Italy and in Scotland), presence of economies of large-scale production in some lines but not in others, existence of transport costs, differences in stock of capital relatively to other factors such as labor and land, and marked difference in the technical possibility of substituting one factor for another in the different industries producing traded products. These factors provide a case for free trade *and* free mobility of factors and one without the other would not secure optimum output in any sense.<sup>4</sup> As we shall see, the implications and importance of these exceptions in a dynamic world can be scarcely exaggerated.

(4) Regarding the balance of payments mechanism, the broad conclusion stands as follows: There is at each point of time a set of equilibrium rates of exchange which will bring international prices in line with each other, reflecting comparative cost advantages adequately and securing multilateral adjustment of balances of payments. The only exception to this is that the market in foreign exchange may be in unstable equilibrium where the price mechanism fails to secure balance of payments adjustment and exchange control may, therefore, be necessary. There is another realistic consideration, empirical content of which is doubted. If the supply and demand elasticities are such that a large degree of devaluation is necessary to secure balance of payments equilibrium, this *may* involve considerable deterioration in terms of trade and loss of real income and may be politically impossible. Recent controversies on the nature of balance of payments adjustments refer to (a) the methodology of the income approach *vis-à-vis* the

<sup>4</sup> J. E. Meade, "Problems of Economic Union," 1953, Chapter 3.



elasticity approach, (b) the magnitude of short-run and long-run elasticities which enter in the equilibration process, (c) the efficacy of periodic devaluations versus a freely floating rate of exchange, (d) what a balance of payment difficulty or disequilibrium really means and whether it is always profitable to view it in monetary terms and as amenable to monetary solutions. In a recent article, Morgan made an attempt in the right direction in trying to link up balance of payments disequilibria with situations obtaining in the goods and the factors-market.<sup>5</sup> As things stand, however, one is inclined to agree with Professor Viner who says, "the modern theory of the exchange rate is not for me a meaningful theory and I see in it no relevance either for the 19th century or for present conditions."<sup>6</sup> Sir Hubert Henderson in an article on the function of exchange rates, written in 1949, shared substantially the same opinion.<sup>7</sup> With analysis of devaluation at its present unsatisfactory stage, I think we claim too much when we suggest that the gold standard fixed exchange rate system was bad because it created deflation *and* unemployment, while the fluctuating exchange rate system is good because somehow it can readjust international price-levels *without* coming into conflict with real wage rigidities and full employment. This is a matter on which there is certainly room for further reflection.

#### THE DOCTRINE OF COMPARATIVE COSTS AND DYNAMIC ECONOMICS

These are our broad propositions in modern international trade theory. The rest are corollaries and controversies. One interesting corollary of the habit of separating monetary from real phenomena is the peculiar logic that devaluation can take care of both a situation of relative unemployment as well as a situation of relative inflation. As Hicks argues in his article cited above, when there is widespread unemployment in one country (extending to export industries, import-competing industries and perhaps to purely home market industries as well) but no serious unemployment in the outside world,

<sup>5</sup> E. Victor Morgan, "The Theory of Flexible Exchange Rates," *American Economic Review*, June, 1955.

<sup>6</sup> Jacob Viner, "International Trade Theory and Its Present-Day Relevance," in Brookings Institution, *Economics and Public Policy*, 1955.

<sup>7</sup> Sir Hubert Henderson, "The Function of Exchange Rates," *Oxford Economic Papers*, January, 1949.

obviously this is the case where wages and prices in the affected country were too high in relation to the world level. "It is not that comparative costs are wrongly assessed, but that absolute costs measured in money are too high all over the country." The trouble could be remedied by a general cut in money wages which would be followed by a fall in internal prices. Keynesian theory agrees but since it stresses rigidity in wage-rates it looks for other solutions, (a) devaluation of currency which has much the same effect as a general cut in wages or (b) a uniform tariff on all imports, the proceeds of which would be used to give a uniform subsidy to all exports—designed to remedy the disequilibrium of money costs without upsetting comparative costs relationships. "Although this infringes the letter of free trade it is precisely in accordance with the spirit."<sup>8</sup>

In another article, his inaugural lecture on the long-run dollar problem,<sup>9</sup> Hicks points out that a uniform increase in the productivity of country *A* with productivity in country *B* constant, will not affect the comparative cost situation. If the increased productivity of *A* is reflected in a uniform lowering of *A*'s prices, the resulting situation is that *B*'s price-level is now too high compared with *A*'s. This is essentially a monetary problem of relative inflation. All that *B* has to do is to devalue her currency in terms of *A* and the situation would be automatically corrected.

The situation, however, becomes entirely different if we deal with three countries or if the growth of productivity of *A* is "import-biased." In the case of three countries, even if *A* has a *uniform* increase in productivity, the growth of productivity and consequent fall of prices in *A*'s "import-competing" goods will cut off *B*'s export market in *A*, *B*'s export-market in third countries and *B*'s home market in her own export goods (assuming that *A*'s supply of these goods are fairly elastic).<sup>10</sup> Similarly to the extent that some of *A*'s exports are competitive with

<sup>8</sup> J. R. Hicks, "Free Trade and Modern Economics," *op. cit.*

<sup>9</sup> J. R. Hicks, "An Inaugural Lecture," *Oxford Economic Papers*, June, 1953.

<sup>10</sup> In a freely "competitive" international economy the distinction between home and export industries is logically unwarranted. Again, as we shall see, if we think in terms of trade in raw materials which are inputs in the production processes, limitation of *domestic* resources need not be a limit to supply elasticities. Again the rate and incidence of technological progress itself contributes to short run increasing returns in various directions. Hicks' assumption of constant costs was therefore not quite suitable for the kind of problem he was discussing.

*B's* rather than complementary, the superior productivity and lower prices of *A's export goods* will cut off *B's* export market in third countries and *B's* home market in import-competing goods. If *A's* exports are complementary to *B's* (i.e., if all national economies are more-or-less specialized and hence growth is inevitably export-biased), relative increase in the productivity of *A's* exports will always be beneficial to *B*. Unless, therefore, we make some assumptions to start with regarding the nature and degree of complementarity or competitiveness of *A's* economy with *B's* and either of these economies with the rest of the world, no logical difference between uniform growth of productivity and import-biased growth can be established. Once import-biased growth succeeds in shutting out foreign exports it may become, unless restricted by inelasticities in supply, an export industry which may carry the war of international competition right into the home and export market of previous exporters whose growth of productivity has not been rapid. One good example is the growth in productivity of the Indian textile industry from an infant industry insecurely protected from Lancashire's competition to a serious rival of Lancashire in the United Kingdom's home and foreign markets. Back in the early stages of the industrial revolution, Great Britain herself developed her textile industry by shutting off entirely her import of Eastern textiles.

The general attitude of economists to this international race for securing comparative cost advantages by technological means (not by beggar-my-neighbor policies of competitive devaluation, competitive tariffs and competitive dumping) is that such competition is beneficial for the world as a whole. The "world as a whole," however, does not at present exist; what exists is a collection of nations. If international competition hurts a number of small nations, each in a different economic sector, this would create a pressure for economic integration, if politically feasible. If the competition hurts in some sectors, a big technologically efficient nation (with ample excess capacity, with a diversified output and with a tolerably high rate of growth particularly in new directions), it is likely to be more or less successful in shifting resources to other industries and gain comparative advantage there. Even in such a case, short-run dislocations may be of a sufficiently serious

nature to justify policies to effect the transition less painlessly than free competition would permit. If international competition or technological substitution hurts an underdeveloped country with a low rate of growth, a narrow range of output and a few "specialized" exports, the economic consequences may be disastrous. If it hurts and hurts badly a country like the United Kingdom with too little excess capacity in the short-run and with an economy peculiarly integrated with international trade, the only feasible remedy may be one of emigration and capital export. And this again may be politically difficult. No doubt, however healthy competition may be (and on this considerable doubts have been raised in recent literature)<sup>11</sup> it is difficult to conceive international competition near full-employment level operating merrily without substantial international mobility of labor and capital. Let us note that whatever competition exists within a domestic economy is very fundamentally due to internal mobility of factors.

While on this topic, we quote a passage from Machlup's article on the dollar shortage in the *Scottish Journal* of October, 1954. Machlup says:

As productivity increases at different rates in different industries and as new products and industries emerge, the comparative advantages which countries have in the production of various goods are being altered and reshuffled all the time. In the course of this process, the scope of international division of labor sometimes widens sometimes narrows. If a country improves its capacity to make products in which previously it has had a comparative disadvantage, the composition of international trade may change, the total gains from trade may become smaller and the volume of trade may shrink. The adjustments to the new productive opportunities may also imply a redistribution of the gains from trade—to the serious disadvantage of some countries—and may force countries to incur considerable costs of adaptation. . . . If such changes in the array of comparative advantages should come in quick succession, one country always initiating the change . . . the chain of losses may be exceedingly tough on the second country. And there

<sup>11</sup> In recent economic literature on customs union, there is a presumption that the more competitive economies are, the more are they likely to gain from free trade. It is however realized that potential or ultimate complementarity is necessary and that competition may not be able to work itself out if there is no factor-mobility between the countries and if different countries follow different monetary-fiscal policies.

is, of course, a good chance that a rich and strong country with plenty of capital to invest in research and development and innovation may come up with a string of new ventures in products that compete with the export industries of a less well-heeled and less dynamic economy. It is in this sense that the faster rate of increase in productivity in the richer and more enterprising country may, if the improvements happen to be competing with the exports of a weaker country impose on the latter a heavy burden of costly and painful adjustments.<sup>12</sup>

As Machlup notes, most of this was envisaged by Haberler in his article on "Dollar Shortage"<sup>13</sup> and in Robertson's book *Britain in World Economy*. The issue—fundamentally one between stability and progress—also comes in again and again in three articles by Viner, Robertson and Haberler on the future of international trade reprinted in the *Readings in the Theory of International Trade*.<sup>14</sup> The line of thought was pushed in a significant direction by Professor Harris's article "Dollar Shortage: Some remarks inspired by Lord Keynes' last article"<sup>15</sup> and Professor Williams in his memorable Stamp lecture and other writings did more than anyone else to demonstrate the irrelevance of the classical static theory of international trade to meet the challenges of the modern dynamic situation.<sup>16</sup>

The problem really hinges on the complementarity or competitiveness of the world economy. Are modern technological innovations of such a nature that advantages of specialization on grounds of different natural resources or different factor endowments have greatly narrowed down? Yesterday, the gap of comparative advantages was said to have been narrowed down by electricity; today we are on the threshold of the atomic age. It is not that these technological opportunities can be utilized by most of the nations simultaneously—it may well be that the gap between relatively developed and relatively

<sup>12</sup> Fritz Machlup, "Dollar Shortage and Disparity in the Growth of Productivity," *Scottish Journal of Political Economy*, October, 1954.

<sup>13</sup> Gottfried Haberler, "Dollar Shortage," *Foreign Economic Policy for the United States*, ed. by Seymour Harris.

<sup>14</sup> *Readings in the Theory of International Trade* (American Economic Association), pp. 497-554.

<sup>15</sup> Seymour Harris, "Dollar Shortage: Some Remarks inspired by Lord Keynes' last article," *The Economic Journal*, June 1947.

<sup>16</sup> In writing this paper I have drawn heavily from the insights, analyses and methodology of Professor Williams' writings and lectures on this subject. See particularly his Stamp Memorial Lecture, 1952.

underdeveloped nations may increase over time.<sup>17</sup> The important question is whether comparative advantage in agriculture can be maintained without industrialization, whether in the face of technological change, specialization in the old primary products would turn out to be bogus specialization. Obviously if skill and technology have become so important a factor of production that the relative importance of other factors of production has greatly decreased, except in relation to it as joint factors, then the time has perhaps come to rewrite our whole scheme of static economic analyses based on consumers' sovereignty, on competition, on variable factor-proportions and indeed revise our whole trend of thinking in marginal terms and give due importance to external economies, indivisibilities, excess capacities, technological change, the size of a nation and its range of products, the economies of earlier start and the economies of experience and such other things.

#### EACKWARD ECONOMIES AND INTERNATIONAL TRADE

The economic world being continuously in a state of flux since the industrial revolution, we will leave aside these disturbing elements of technology on which predictions are scarcely possible over time, and take a brief view of the literature on underdeveloped countries in relation to international trade. In the preceding discussion on differential rates of productivity, we have assumed that productivity increases are fully reflected in fall in prices, keeping money incomes constant (but of course raising real incomes) and we have judged the consequences of this fall in prices on international price-structure, exchange-rates and balance of payments. But what, it may be asked, about the income-effect? Will not *A*'s imports from *B* rise if *A*'s productivity and therefore her real income rises? That depends on the direction of growth of *A*'s economy—whether in the course of her growth, her economy has become more complementary or more competitive with *B*'s. If *A*'s growth is import-biased *vis-à-vis* *B*'s economy, *A*'s imports from *B* cannot, by definition, rise. In other words, in relation to *B*, *A* is getting more and more self-sufficient, while

<sup>17</sup> Thanks to the unequal pace of development, world real income per capita was perhaps less in 1950 than it was in 1900. Cf., Singer, "Economic Progress in Underdeveloped Countries," *Social Research*, March, 1949.



for *B*, self-sufficiency (via tariffs, import-controls and real income cuts) with regard to *A* and possibly third countries, is forced on her by the pressure of circumstances.

Hicks has tried to show that, historically, growth is at first export-biased and later becomes import-biased. The thesis that with growth, the ratio of imports to total income falls, is statistically verified for the U.K. and the U.S.A. This has been used for various types of arguments. Professor Kindleberger used the idea for a model arguing that all countries pass through a sequence of stages, starting out as a borrowing debtor with increasing import-surplus, becoming a lending creditor with increasing export-surplus and then reaching maturity as a mature creditor with an import surplus. This raises various theoretical and empirical problems which bear on the relative immobility of international capital nowadays, the difficulty of defining a mature nation and an underdeveloped one—the marginal efficiency of investment may be higher in the United States than in an underdeveloped country, etc. In a recent article Hla Myint points out that many underdeveloped countries started out after the opening up period with an immediate export surplus.<sup>18</sup> Whatever its implications on the actual direction of or (welfare) need for international movements of capital, there is considerable evidence that the ratio of imports to total income and import of primary products to total imports for the U.K. and U.S.A. has had a downward trend. Henry J. Bruton shows that this may be due to import saving technological changes, the increasing share of domestic services in the consumption of developed economies and other reasons. The consequence of this, to quote Bruton, is that

if exports are the sole source of exchange-earning power for an underdeveloped country, the percentage rate of growth of income for this country must be less than that for the developed countries. . . . Without capital imports, therefore, the underdeveloped country will be unable to achieve the rate of growth of income of the developed countries. A rapid growth of income in the developed country is necessary to keep the percentage rate of growth of the underdeveloped country's exports from declining; but this means that the absolute difference between the incomes of the developed

<sup>18</sup> Hla Myint, "The Gains from International Trade and the Backward Countries," *Review of Economic Studies*, 1954-55.



and the underdeveloped countries will increase and the latter will fall further and further behind.<sup>19</sup>

This is not considered as a problem by many economists; Machlup<sup>20</sup> would say we should distinguish between a *net* loss of income and a *retarded* increase in the growth of income; Harry Johnson<sup>21</sup> would say that though a uniform increase in productivity in country *A* may hurt country *B* because of the latter's adverse terms of trade with *A*, this is like complaining why *A*'s rate of increase of productivity should not be still higher to offset this loss! Bruton himself argues (and we fully agree with him) that the problem of effecting economic growth essentially depends on domestic technological achievements.

There are some economists who are inclined to be more optimistic about the future of primary producing underdeveloped countries. Now it is difficult to generalize about underdeveloped countries just as it is difficult to generalize about so-called "mature" economies. In general, a nation is always likely to gain by exploiting (if it can efficiently) its internal resources instead of exporting its raw materials and buying a part of the finished product from the importer of its raw materials. A small underdeveloped nation, however, would find it difficult to utilize its own resources to produce a large number of commodities at sufficiently low cost, partly because its resources are limited and partly because its limited internal market does not afford opportunities for large-scale production. (This was not a problem for a small country like Great Britain in the early days of industrialization for reasons we are broadly aware of.) A small, underdeveloped country like Burma with considerable natural resources (not mutually complementary), little skill and a low population density, may have to depend (and may find it profitable in depending) on international trade for growth, to a large extent. It is this basic consideration which *hides* behind Hla Myint's recent article on the gains from international trade and backward

<sup>19</sup> Henry J. Bruton, "Growth Models and Underdeveloped Economies," *Journal of Political Economy*, August, 1955, pages 322-336.

<sup>20</sup> Fritz Machlup, *op. cit.*

<sup>21</sup> H. G. Johnson, "Increasing Productivity, Income-Price Trends and the Trade Balance," *Economic Journal*, September, 1954. See also his "Economic Expansion and the Balance of Payments," *Bulletin of the Oxford Institute of Statistics*, February, 1955.

countries. Hla Myint attributes low gains from international trade reaped by some underdeveloped countries to peculiar imperialistic factors which are absent today and envisages the possibility of high-wage production of primary products for export, at favorable terms of trade, to manufacturing countries. He concludes that there is no basic advantage in industrialization and advantages from agricultural development should not be underrated. The question, however, is not whether primary production should be given up, but how far the economy can be diversified and primary products or their export-receipts domestically utilized for manufactures.

Bearing on this is Dr. Singer's thesis of the colonial nature of foreign investment in extractive industries in underdeveloped countries and its consequences on the distribution of gains from trade. There is also the quite distinct thesis of MacDougall in his "Lecture on the Dollar Problem"<sup>22</sup> where he predicts that U.S. exports are potentially vulnerable and U.S. imports are potentially explosive. Similarly, Aubrey<sup>23</sup> predicts that the downward trend of U.S. import-income ratio may not continue in the future, so that primary producing nations are likely to benefit from specialization if the elasticity of their supply is increased as demand for their product rises. These are interesting, plausible but largely speculative hypotheses and it is difficult to be dogmatic one way or the other.

The view, broadly speaking, is generally taken that the case for protection of underdeveloped countries rests mainly on the existence of unemployed or underemployed resources. From the point of view of comparative costs and optimum allocation of world's resources the issue simply is whether through protection and other technological means, larger output is ultimately produced at lower costs of production. The important points to investigate, therefore, are the factor endowments of a country, its level of skill formation, how far its factors are unemployed or underemployed, how far through technological means its factor-supply position can be improved and how all these are likely to affect its international trade relations with other na-

<sup>22</sup> Donald MacDougall, "Lecture on the Dollar Problem," *Economica*, August, 1954.

<sup>23</sup> Henry G. Aubrey, "The Long-er-Tm Future of United States' Imports and Its Implications for Primary Producing Countries," *American Economic Review*, May, 1955.

tions. As we shall see presently the static framework of comparative cost theory does not permit consistent analysis along these vitally important lines.

#### THE IMPACT OF TECHNOLOGY ON RESOURCES AND FACTOR-PROPORTIONS

An important matter, therefore, is the nature of unemployment in labor and resources that exists in a particular economy. Are the excess capacities in various directions complementary so that they provide scope for their combined utilization and growth? The Ohlin argument for specialization in each region according to factor-endowments obviously assumed free variability in factor-proportions. This provided the fundamental basis for his argument that free trade will *tend* to equalize factor-prices and hence will be equally favorable for all regions. We know, however, that factor-proportions are not freely variable, so that super-abundance of a factor like labor in a particular region may well be a handicap both for its growth as well as for its trade. In India, labor is the abundant factor and there is a deplorable tendency of its getting more and more abundant year after year. What are the labor-intensive products in which, under modern industrial conditions, India would have a comparative advantage in specialization? We cannot think of any, except handlooms and handicrafts which have very little international demand, and, of course, domestic services of various kinds which cannot be exported. The lack of sufficient capital and land has nullified our comparative advantage in most lines of agriculture and industry. International trade has a pull on our scarce factors, our climatic advantages in jute and tea, etc., rather than on our abundant factor, labor. Indeed the obligation to maintain full employment complicates our technological efforts. Technological progress is essentially labor saving. Indeed the use of labor-saving devices in the industrial revolution in England is largely explained by the pressure of foreign demand on existing techniques of production. The technological progress of the U.S.A. is similarly explained by a shortage of labor in relation to resources. Yet in a country like India, technological progress and growth of output are likely to be associated with substantial technological unemployment. This is well explained in an

article by R. S. Eckaus.<sup>24</sup> As with labor, so with natural resources, sheer abundance is no advantage in growth or in trade.

Here again it was the scarcity of some resources at a point of time rather than their super-abundance which provided the impetus to technological progress. Resources cannot be conceived in a static framework. What would turn out to be a valuable resource itself depends on technological progress. Take the case of hydro-electricity or of uranium. Again, scarcity of one resource may lead to the discovery of a better substitute. The impetus to coal mining in England was given by a growing shortage of firewood. The need for draining water out of coal mines and the need for safe lighting in the coal pits helped the discovery of steam and gas respectively. With the development of steam power, coke and iron smelting, came the railways. One innovation called for another and the diffusive influence of technology worked all round. The availability of natural resources within the national boundary is not by itself helpful for growth and technological progress. Indeed it may be a deterrent. British demand for Swedish timber for ship-building prevented Sweden from turning her attention to industrialization till the use of iron ships in England depressed Swedish exports and forced her to take industrialization more seriously. Technological progress is as much a result of pressures as of opportunities. True opportunities may be often lost and pressures may not create timely responses. The entrepreneurial factor and social institutions are, of course, very important.

Again early industrialization was considerably helped by foreign trade. It was foreign trade of a peculiar type. The free trade which in a *static* theory is held necessary to secure "efficiency" or consumers' sovereignty is a trade in finished consumption goods. The *dynamic* pattern that trade actually took was largely a trade between primary products and finished manufactures. The export of primary products which are *inputs* in the productive process should logically be treated as export of natural resources or factors of production—it was not a mutual exchange of finished utilities. Exports of factors of

<sup>24</sup> R. S. Eckaus, "The Factor Proportions Problem in Underdeveloped Countries," *American Economic Review*, September 1955.

production are logically ruled out in international trade theory but as Meade has pointed out mobility of factors internationally may be necessary in case of joint demand for factors. Raw-materials had to be combined with skill to produce manufactured goods. Skill is part of technology. Technology set the pace and the pattern of the movement of goods and factors followed. With colonies in their low stages of technological development, they could not, as Ohlin would have wanted it, specialize in the production of goods in which they had their natural resource advantages. Again, the relation of technology with all the other available factor-endowments within a nation, or outside it, is not very clear. With reference to different resources technology may be at the same time resource-creating, resource-economizing, resource-utilizing and resource-substituting. In a dynamic economy no neat generalization about national endowments believed to be existing at a point of time can be made. We would be inclined to consider national natural resources, actual and potential, as important passive factors reacting in diverse ways to the impact of technological change. There is a complex kind of two-way interaction between technology and resources and no analysis which ignores technology and takes a point-of-time stock of existing resources is likely to be adequate in a dynamic economy.

But what greatly reduced the value of the Ohlin type of analysis, in terms of regional factor endowments, was not only the neglect of the basic dynamic factor, technology, but the implicit assumption that all regions are equally developed technologically. If regions are in different levels of technological development, labor, capital (and even land and natural resources to the extent that they are man-made) cease to be inter-regionally comparable. Thus due essentially to the technologically inefficient content of our labor and capital in India we use more labor, more capital, perhaps also more raw material resources per unit of output in most of our better-organized industries than is used in similar industries in the U.K. or the U.S.A. Note that we do not use more capital per unit of labor. Indeed the use of more capital per unit of labor may be one of the visible criteria of technological progress. In spite of this disadvantage, we do compete with England in some industrial products, particularly textiles, but that is precisely

because our wages are very low compared with wages in the U.K. With production functions different, due to different levels of technology, it is impossible to go behind domestic prices to factor prices, compare them internationally and posit a rate of exchange which equates the prices of goods and by so doing has the tendency to equate the prices of factors between the two countries. Nor is this a problem peculiar to underdeveloped countries—there are degrees of underdevelopment regarding technological achievements and the Leontief paradox on the structure of American foreign trade throws interesting light on this discrepancy.<sup>25</sup> The superior joint efficiency of labor and capital, their right proportions as well as their right quantity along with rich entrepreneurial and natural resources is partly reflected in higher wages, partly in lower prices, partly in a wider range of products and partly in new products. All this gives a comparative advantage over a wide range of commodities which is basically technological and increases its competitive power. If a high-cost, high-living country can compete effectively with a low-cost, low-living country, it is because of its superior technological level which made it a high-living country in the first place. The proper way to compete with such a country is not by tightening the belt as the United Kingdom is trying to do with so much uncertain success, trying to hit private investment on the head every time a so-called balance of payments crisis occurs and trying to throw all the responsibility for inflation on labor unions who after all are willing to produce more if they can earn more (we cannot have private enterprise if we stifle profit-motive all round, the profit-motive of the wage-earner as well as the profit-motive of the entrepreneur). The proper way is to increase technological efficiency in feasible directions, or if that is not possible, to get lost in the Commonwealth through emigration and "foreign" investment.<sup>26</sup>

<sup>25</sup> Wassily Leontief, "Domestic Production and Foreign Trade: The American Capital Position Re-examined," April, 1953.

<sup>26</sup> If ground lost in technological efficiency is sought to be regained by temporarily raising tariffs and by other *interim* measures to raise productivity, its competitors who are likely to be hurt in the end are likely to retaliate by similar policies. This is analogous to the Scitovsky case of dynamic oligopolistic "competition." In the monetary field this is easily reflected by the fact that a balance of payment surplus of a country is the reflection of the balance of payment deficit of another.



## SUMMARY AND CONCLUSIONS

To sum up our arguments: The original theory of free trade was based not on considerations of the advantage of international competition but on considerations of mutually beneficial specialization. Not only was international competition not envisaged, it was directly ruled out by the assumption that factors of production were internationally immobile. True, the achievement of specialization was sought through competition, but *continuing* dynamic competition was not envisaged and the process through competition and free trade to specialization was considered to be a once-over process. Technology and growth considerations were largely ignored and the static welfare argument for free trade which had had logical relevance only to trade in finished consumers' goods was applied to a case of complementary trade in raw materials, i.e., inputs, in exchange for manufactures, i.e., finished products. A special theory of inter-regional trade on the basis of comparative costs was held necessary because factors were considered to be inter-regionally immobile. Trade in goods was considered by Ohlin to be a good substitute for free mobility of factors. There was an implicit assumption in Ohlin of free variability of factor proportions and an equal level of technology in all regions for otherwise factor endowments in different countries become incomparable and rigidity in techniques makes full-employment of factors within a region either impossible or subject to different degrees of disguised unemployment or different degrees of inflationary pressures in different regions. Ohlin's theory is also largely static. There was a once-over assessment of national resources (land, labor and capital) and the creative influence of technology (though not of trade itself) in relation to all these other factors of production was ignored. Yet, the higher the level of technology a region has, the more rapid is the possibility of its further technological progress, unless institutional and resource barriers operate against it persistently over time. Technology is the greatest external economy industry, its advantages are diffusive. It breaks through the rigid dichotomy between agriculture and industry and between one sector of industry and another. In short, it is a force making for diversification of output rather than narrow specialization. It is easy to understand that if growth is stopped,



new products are not thrown out and technological progress is kept at a standstill in all nations, complete free trade (without tariffs, without import controls, without significant inter-regional factor mobility) might ultimately secure complete or more or less complete specialization on lines of comparative advantage. I am not sure if world efficiency and output will invariably be maximized this way. Even if it is so, many nations would lose in the process due to the complementarity of factors in production and the varying strength of reciprocal demands for different imports and exports, in the *ex post* specialized situation. This will raise problems of compensating the losers. If such compensations are difficult to organize internationally and if, in spite of it, international competition is forced upon technologically weaker nations—nations pledged to full employment, nations with their factors tied to their soil by nationalism—then the pressure of international competition will itself lead to a strengthening of direct controls and perhaps a slow corrosion of private enterprise—not in technologically advanced countries as Marx predicted but in technologically deficient ones. Yet even outright socialism will not solve the basic problems at issue which hinges on international competition.

These conclusions follow from broad, theoretical observations and may not have obvious relevance to the particular situation of the world today or in respect to any particular country. We have over-emphasized problems which appear to be more important and have tried to envisage long-run forces which we are sure operate over a succession of short periods. If the prospects of free trade today do not appear particularly hopeless, it is because we are inclined to think of dynamic problems in international trade as simply a balance of payments problem and also because we have bolstered up our national economies with a great deal of tariffs, quotas, agreements, bilateralism, discrimination, regional blocks and internal and external controls of diverse kinds and *not* because we have tried free trade and found that it worked. In the 19th century world where it is believed to have worked well, it violated most of the economic, social and political values we consider desirable (today) and it violated also the basic logical presumptions of free trade economic theory. Apart from the

fact that the "free trade" we had was more a gold-standard convertibility rather than absence of tariffs, there was associated with 19th century trade a series of significant exogenous factors which had no relation at all with the "logical" case for free trade. There was imperialism, there were wars for raw materials and markets, there were trade cycles, deflation and unemployment, there was considerable international mobility of factors of production, there was an unequal trade between inputs and finished products. And that is a world which is fast disappearing. Until we can devise more balanced blocks of integrated economies of more or less equal economic weight, or, what is better, promote greater international mobility of labor, capital and technology, it would we think be too risky to try free trade in the right text book spirit.

The conclusion our analysis leads to is that the case for international *cooperation* today does not need any value judgment. Indeed under the pressure of economic circumstances, value judgments have continuously changed and it is impossible to predict what value judgments we will have in the centuries ahead. One thing, however, demands scrutiny, by economic logicians as well as by political philosophers—and that is a possible conflict between accepted values. Private enterprise, competition, growth, full employment, free trade, national boundaries (with all their consequences in separate currency, restricted factor mobility, independent monetary-fiscal policies) are perhaps all good things to have, but economic theory has not provided any logical synthesis of all these elements. Freedom, as Professor Samuelson remarked (in a recent article in *The Three Banks Review*), is a scarce commodity and some freedoms have to be sacrificed in some direction to achieve more freedom in others. In the task of effecting that compromise, the economic logician can play his part; but a tolerable synthesis can only emerge when the conflicts in our value judgments are made clear and all social scientists and the common man participate in effecting the necessary compromise.



**PART II**  
**PLANNING AND LEGISLATION**

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## CENTRAL PLANNING OF INVESTMENT IN GREAT BRITAIN<sup>1</sup>

*Peter M. Gutmann*

### INTRODUCTION

THIS is an essay in the practice and theory of central planning of investment in Great Britain during the critical years 1947-1951. It analyses the structure of the investment planning mechanism, the use of physical investment controls, the methods of limiting and allocating investment, the criteria of choice formulated to determine which programs were to go forward and which not, and the meaning, success and limitations of this sort of planning.

At the end of the war, demand for resources in Britain considerably exceeded supply. This was true of all types of resources but particularly for those used in construction of investment goods. With full employment, more of one thing meant less of something else. It was clear some demands would have to go short. The important question was "which ones?"

The gap between resources and requirements will in the end be closed by some of the requirements being left unsupplied. But if the process of closing the gap is left to chance, some vital requirements are sure to be squeezed out by the less essential . . . the economic budgets must balance themselves ultimately, for it is impossible to consume more than is produced; the real question is how the balance is brought about.<sup>2</sup>

The need to allocate limited resources amongst competing claimants was not unforeseen. Success of wartime planning for national objectives did much to foster the will to continue conscious direction of resources to achieve specific objectives. The 1944 Coalition Government White Paper on Employment Policy noted that in the transition period, the Government is

<sup>1</sup> Research for this essay was conducted in part through a series of interviews while the author was a research student on a Fulbright grant at Cambridge University. He wishes to thank all those who so cheerfully gave of their time and effort to discuss with him Britain's planning. He also wants to express his appreciation to professors Marcus Fleming and Abram Bergson who perused the manuscript and made a number of fruitful suggestions.

<sup>2</sup> *Economic Survey for 1947* (Cmd. 7046), p. 7.

resolved that, so long as supplies are abnormally short, the most urgent needs shall be met first. Without some of the existing controls this could not be achieved; prices would rise and the limited supplies would go, not to those whose need was greatest, but to those able to pay the highest price.<sup>3</sup>

At the war's end, there was uncertainty which controls were to be retained. The wartime planning organization was continued in attenuated form under Herbert Morrison who headed the Lord President's Committee of the Cabinet. The structure became decentralized, not well coordinated, without adequate staff or conception of the prerequisites of planning. Economic budgets were formulated for manpower and national income and expenditure with some attention to the balance of payments; real concern with particular problems of steel, timber, fuel and power, and other material shortages began only early in 1947. The structure suffered from division of responsibility between Dalton with fiscal policy at the Treasury, Cripps, spurring exports at the Board of Trade and Morrison planning the home economy through the Lord President's Committee and the Home Economic Committee of the Cabinet. Coordination lagged on investment as elsewhere.<sup>4</sup>

The coal crisis set back production in February 1947. Convertibility provisions of the U. S. loan were suspended with the foreign exchange crisis of August 1947. Moreover many build-ings were being started, few completed due to lack of over-all housing investment control. Radical revision was needed in planning organization.

Sir Stafford Cripps became chief planner, first as Minister of Economics, soon thereafter as Chancellor of the Exchequer. A Central Economic Planning Staff with administrators and economists was formed the summer of 1947 to aid coordination of economic policy. It was placed under Cripps and then transferred to the Treasury January 1948. The Treasury became the center of the planning structure. Starting in 1947, the

<sup>3</sup> *Employment Policy* (Cmd. 6527, 1944), pp. 9, 10. The White Paper stated also that "use of capital will have to be controlled to the extent necessary to regulate the flow and direction of investment . . . to ensure the proper priorities," but this referred to access to the capital market more than physical controls over investment.

<sup>4</sup> Samuel H. Beer, *British Planning under the Labor Government*, *Social Research*, XVII, 1, March 1950, passim; Herman Finer, *The Central Planning System in Britain*, *Public Administration Review*, VIII, autumn 1948, passim.



government made decisions about the size and distribution of investment.

#### INVESTMENT ALLOCATION

Central in the determination of size and distribution of investment, to the extent that the government exercised control, was the Investment Programmes Committee (IPC).<sup>5</sup> This was a unique committee in administrative practice; its members were selected not as Departmental representatives but as individuals on the basis of personal capacity and knowledge. Some were administrators and some economists, some "planners" and some "liberals" in varying degrees. The four or five members were chosen by the Chancellor of the Exchequer from the Central Economic Planning Staff (as chairman), the Economic Section of the Cabinet Offices, and some Ministries which sponsored a good deal of investment, namely the Ministry of Supply, Ministry of Works and Board of Trade.

Unlike other interdepartmental committees, the members carried no instructions from their Departments and were not responsible to them. It was a close approach to a committee of disinterested experts to advise the Chancellor of the Exchequer. It had no executive authority though in practice its powers within its sphere of operations were extensive. Recommendations were framed on a unanimous basis, though it was in theory possible for one member to write a note of disagreement on any issue. On technical matters it was aided by staffs of Departments.

General policy aims established by the Cabinet left much to interpretation. From its inception in 1947, the Committee was instructed to frame investment programs consonant with government aims to secure (a) full employment without inflation, (b) "adequate" balance of payments, (c) "due" provision for investment, (d) generally rising standards of living, and (e) fulfillment of major "political" objectives as housing or defense. Sometimes instructions were more specific. At one time the Committee was directed to reduce investment £100 million from the previous year. But it was not stated whether this meant reduction from the beginning, end, average, or peak of that year.

<sup>5</sup> Referred to as IPC hereafter.

*Supply of Investment Resources:* First, physical resources available for investment had to be determined. This involved prediction, since each year's estimates were framed the spring preceding. This was done by an interdepartmental technical committee, the National Income Forecast Working Party, containing representatives of Central Economic Planning Staff (as chairman), Economic Section of the Cabinet Offices, Central Statistical Organization, Treasury and several Departments.

Potential supply of investment resources was estimated from (a) expected output of building and civil engineering industry, based on building materials (timber, bricks, steel, etc.) and labor estimated as available and (b) expected output of machinery, plant and vehicle industries based on material supplies (notably steel), labor and import availabilities. Past input-output figures were adjusted for a productivity trend. The necessary data was received from the Ministries of Works and Supply and the Board of Trade.

Obviously estimates depended on predictions of (1) productivity increases and (2) "exogenous" factors which in turn affected the former. "It is very difficult to forecast growth of productivity," said the *1950 Economic Survey*, "and the figure which has been taken is more an assumption than a forecast."\* The *Economic Surveys* underestimated productivity increases through 1950.

Predictions of home production and productivity depended on material availabilities. These were subject to exogenous factors. A severe winter, as in 1947, impeded production due to lack of coal. Increased German needs could cut foreign scrap available. A shipping shortage could lower iron ore imports. Heightened production and stockpiling abroad could reduce copper supplies. Predictions also depended on labor availabilities. Since there was practically no direction of labor, working force distribution was difficult to estimate. Labor bottlenecks holding back production, e.g. coal, had to be forecast. Some estimate was required for industrial disturbances which in turn hinged on inflation and a whole host of factors. All this was required nine months before the beginning of the year under consideration.

\* *Economic Survey for 1950*, p. 19.

Resources "available" for investment were determined thus: from calculated home availabilities were subtracted exports and added imports of investment resources which depended in part upon the state of the balance of payments.<sup>7</sup> Then, deduction was made for defense and consumption needs. The latter included some automobiles, metal goods, several types of repairs. The rest was available for investment. "Available" implied many predictions and policy decisions on imports, exports, consumption, etc.

*Demand for Investment Resources:* About January of each year, the IPC requested Departments to present "investment programmes" of industries under their sponsorship. The Ministry of Supply was in charge of producers goods industries, the Board of Trade of consumers goods industries, the Ministry of Fuel and Power of petroleum and nationalized coal, gas, electricity, the Ministry of Works of government and some other building, etc. Early in 1950, for example, Departments presented 1951 programs in some detail, estimates of 1952 and 1953 requests, and reports on actual 1949 investment. Estimates of investment demand a year in advance were not easy due to considerable variation in information available to Departments and the extent of control exercised over different sectors.

Programs submitted to the IPC comprised (1) actual programs of (a) government, (b) nationalized industries, (c) private sector and (2) extrapolations of preceding years' investment trends (adjusted for expected deviations) for that part of the private sector for which no actual plans were known.

Some investment, as building work by the Armed Services or Ministry of Works for the government was completely controlled. Plans were known. A second group, as much of the housing as well as the university building and educational construction, depended partly on government grants to Local Authorities and others. Plans could be influenced by varying grant conditions and by admonition. Future requests for investment allocation were known fairly accurately. A third group embraced nationalized industries—coal, gas, electricity,

<sup>7</sup> Which was a function of foreign demand, terms of trade, U. S. aid, etc. Imports also depended on the level of internal demand, as modified by fiscal policy and import controls.

transport, iron and steel (even before the temporary nationalization), etc. Investment plans were made long in advance and accurately known. They were susceptible to some government control. In 1950 a little more than half the total national investment was undertaken by the "public sector" (if we include iron and steel).

In the private sector, investment plans of large firms, as I.C.I. or Unilever, were accurately ascertained. Industries with strong trade associations which collected data from members likewise had programs fairly well known. Departments carried on lengthy conversations with trade associations and large firms to ascertain plans, discourage the non-essential in advance, suggest investment in some sectors, discuss planning methods and effects, and keep in touch with private industry. But for the many small, scattered firms Departments had little information. Future investment demand was estimated by extrapolating past trends (calculated from sample surveys) with allowance for obvious modifying factors; likewise for future building repairs.

We can also distinguish between building construction investment and repairs above the license limit, building repairs beneath the license limit and machinery investment. Future demand for building construction investment was estimated with fair accuracy, but each Department had to request from the IPC building license allocations for its sector before any applications for licenses were made to it. Departments dealing with private industry could only estimate subject to some error. Investment actually undertaken was well controlled through building and repair licenses. Building investment in repairs beneath the license limit was difficult to estimate and not subject to direct controls.<sup>8</sup> Future demand for machinery investment was partly approximated from past trends, partly from plans. It was not subject to direct controls other than import limitations and government persuasion of manufacturers to export.

The allocation process was time consuming; there were some forty separate programs. Each Departmental representative appeared before the Committee as supplicant for investment in his sector, aided by specialists (on rails, canals, etc.). For

<sup>8</sup> Other than timber allocations where timber was required.

Ministries sponsoring nationalized industries, someone appeared from the latter but only as an expert. The program was agreed to by a Ministry and a nationalized industry beforehand. "Under present practice (late '50)," one planner held, "the case for each individual investment 'programme' is usually based largely on qualitative arguments supported perhaps by statistics of the expected increase in output."<sup>9</sup> The IPC sought capital-output figures but often industries did not know them.

*Total Amount of Investment:* First of all, the total quantity of investment had to be determined. It related to gross rather than net investment, for additions and replacements both use up resources of materials and labor and both produce inflationary effect through creation of incomes without equivalent consumption goods and services. Some important repairs and maintenance were included but procedure varied. Railroad track maintenance was considered "investment" only for a time. Exact delineation between "maintenance" and "gross investment" had to be arbitrary to some extent.

Total investment can be determined through either market mechanism or physical controls. During this period it was largely determined through physical controls. Two possibilities appear. One, physical shortages may limit investment of different types, possibly the total. But to a degree it can always be increased by cutting exports of investment goods and taking from consumption and exports materials in shortage such as metals. To this extent the investment total is "political" despite limiting shortages. Two, if there are no physical limits, total investment being determined by the willingness of the community to forego present consumption, "determination of the rate of investment is unavoidably political."<sup>10</sup> The community decides it through elected government.<sup>11</sup> In 1950, for example, with few specific bottlenecks, the IPC limited the total. In 1951 it presented alternative programs with different totals to Ministers who made final decisions.

As for the result, one planner thought that "at the present time (late '50) the total of investment seems to be intended to

<sup>9</sup> From an unpublished paper by Mr. Robin Marris, now of Kings College, Cambridge University.

<sup>10</sup> Abba P. Lerner, *The Economics of Control*, p. 262.

<sup>11</sup> To the extent that government exercises control through direct limitations, controls on foreign trade, fiscal and monetary policy, etc.

be the maximum that can be managed without serious inflation and without the government being voted out of office because consumption is too low."<sup>12</sup>

*Sectoral Distribution of Investment:* The investment total was allocated among sectors through physical controls, not a market rate of interest. There were several reasons.

(a) Most important, during this period reliance on an interest rate alone would have caused either inflation or misallocation of resources or both. Price controls were necessary to prevent inflation<sup>13</sup> (and regressive income redistribution). But price controls limit costs of some materials and not others. They make investment in certain sectors very "profitable," in others (as basic industries with price fixed products) "unprofitable." A high interest rate weeds out the wrong programs.<sup>14</sup> A low interest rate produces a scramble for limited resources which prevents completions<sup>15</sup> and exerts upward pressure on prices.<sup>16</sup> The choice between inflation and misallocation of resources was unsatisfactory—hence, reliance on physical controls.

Other reasons were considered of some importance. (b) A rate of interest is significant only in relation to the private cost of capital investment. In so far as social cost deviates from private cost, the interest rate is not a good investment criterion. (c) A high interest rate tends to eliminate sober rather than speculative investment. Projects with a small chance of a large return crowd out projects with large chance of smaller return. (d) A rate of interest is significant only in relation to an expected rate of return. Expectations of a demander of capital goods are based on limited knowledge. A central authority may have more information, be a better judge of future returns and more capable of allocating investment. (e) The interest rate reflects relative social urgencies only under "equitable" income distribution. If this cannot be achieved, e.g. due to

<sup>12</sup> Marris, *op. cit.*

<sup>13</sup> Due to price-wage spiral. A stable equilibrium would have been difficult if price controls had been removed.

<sup>14</sup> Interference with one part of the price mechanism (through price controls) makes some other part (e.g. the interest rate) a bad indicator of social needs.

<sup>15</sup> For such a scramble note the case of housing in 1947.

<sup>16</sup> Even a high interest rate might not have prevented a disastrous scramble for materials, insofar as firms were self-financing and not deterred by high interest (liquidity was high). Moreover, if firms believe prices will rise sufficiently, even high interest rates might be no deterrent to borrowing; it may be cheaper to expand immediately than wait.



necessity for labor and business incentives to reward effort and the need for a return to owners of private capital required if private enterprise is to be maintained, the "votes" of some members of the community will be inadequately represented in an interest rate-capital allocation mechanism. (f) To an extent, capital rationing by lenders rather than the interest rate itself determines the allocation of investment in the market mechanism.

Since demands for investment always exceeded available physical resources or over-all financial limits imposed, the IPC had to cut investment requests. For this, criteria of judgment were developed.

(a) internal consistency of programs: It examined each major program submitted, in the light of general conditions, for internal self-consistency.<sup>17</sup> For 1950 for example, over protest of the British Electricity Authority, it cut transmission and distribution programs as being too great in relation to possible increases in generating capacity.

(b) feasibility: It determined whether physical materials could be secured.<sup>18</sup> If not, then all parts of the program dependent on such materials were cut. The British Electricity Authority once planned generating capacity increases requiring more boilers than the boiler industry could supply. The industry had overstated its capacity. As a result, the generating program was cut.

(c) completion of maximum number of projects: It allocated resources to secure completion of some projects rather than starting so many as to leave all partly unfinished. By 1947 too many buildings had been begun.

It was necessary to bring the actual investment plans into better balance with the remaining resources. For it was plain that more was being started than could be achieved in a reasonable time, so that periods of construction and manufacture were lengthened.<sup>19</sup>

<sup>17</sup> The problem of consistency was in reality broader than that of "balance" alone. There remained a double question. Could the aims be achieved given the materials? Were the materials needed to achieve the aims? In general, the IPC could do little to check whether technological coefficients (output per capital input) were estimated correctly since relatively little information was available on the subject. Nor was the IPC equipped to undertake checks. It usually accepted estimates of Departments in charge of industries.

<sup>18</sup> Completion of projects depended both on correctness of forecasts on materials available and on stock of materials which could be depleted.

<sup>19</sup> *Economic Survey for 1948* (Cmd. 7344), p. 38.



For 1948 resources were concentrated on projects already well under way. Buildings less than 25 per cent completed were stopped, individually reviewed and licenses granted only to the essential. "In 1948 work in progress was brought into a proper relation with the rate at which it could be completed."<sup>20</sup> "During 1949 a further reduction in the volume of unfinished housing work took place."<sup>21</sup>

(d) national policy: It allocated investment to sectors of greatest national urgency. Each year, the *Economic Survey* published tasks for the succeeding year. Investment was permitted for projects which (1) surmounted shortages of basic materials as coal, iron and steel, electricity, sulphuric acid, and other materials and services basic to national effort, (2) increased exports, material and invisibles, (3) saved imports, (4) promoted research, new products and development to keep up with competition abroad, (5) yielded rapid and considerable cost decreases.

In April 1949, the Chancellor of the Exchequer issued a further memorandum of guidance . . . emphasizing the need to exercise restraint over capital expenditure, and stressing the importance of giving preference to increases in capacity designed to overcome shortages of basic materials, to projects which were likely to increase exports to, or save imports from, hard currency countries on a substantial scale, to the promotion of technical developments and practices, and to proposals which would yield marked and immediate reductions in costs.<sup>22</sup>

In addition, investment was granted for (6) defense, (7) welfare, including housing and hospitals, (8) other government projects such as offices.<sup>23</sup>

There were no absolute priorities. "The comparison between programs and the final allocation is made purely on the basis of qualitative judgments."<sup>24</sup> Such was the opinion of one planner. Allocations depended on conditions at the time. Basic indus-

<sup>20</sup> *Economic Survey for 1949* (Cmd. 7647), p. 4 also cf. *Capital Investment in 1948*, p. 6.

<sup>21</sup> *Economic Survey for 1950, op. cit.*, p. 51.

<sup>22</sup> *Ibid.*, p. 7. These instructions were issued to the Capital Issues Committee (which passed on applications for bond flotations, etc.) but likewise held for the IPC.

<sup>23</sup> Investment had to be balanced as between sectors.

<sup>24</sup> Marris, *op. cit.*

tries, export stimulation and import saving received emphasis. In practice,

in the various cuts in the last three years, the element of less essential investment has almost certainly been reduced to a level which represents, if not the economic minimum, probably what is regarded as the political minimum.<sup>25</sup>

Some complained that "non-productive" investment got too great a share. Britain put 56 per cent of investment into agriculture, industry and transport compared with France's 77 per cent; 44 per cent of the total went to welfare services and housing.<sup>26</sup> This was a "political" decision of government and public over which the IPC had little control.

What was "essential" occasioned dispute. Some held that more should have gone to manufacturing, less to "basic" electricity expansion.<sup>27</sup> The IPC maintained its criteria. In addition, Departments presenting large, well-formulated programs may have been able to secure larger investment allocation proportionately than those with dispersed industries whose future investment demand could only be estimated roughly. But the latter were less important in national objectives.

(e) long run vs. short run yield of investment: In 1947,

the most important projects on the industrial side are those which yield a quick return in terms of increased output per man year, especially in the undermanned industries. Long term projects must inevitably take second place to projects which will quickly help to solve the special difficulties which are limiting the expansion of the total national production and are distorting its balance.<sup>28</sup>

Available resources must be concentrated on those projects which will make the best and quickest contribution to the balance of payments.<sup>29</sup>

Emphasis on rapid yield subsided with the recession of a need for quick returns. Oil refineries, steel mills and other long term projects were constructed (some even from the beginning). As

<sup>25</sup> E. A. G. Robinson and A. D. Roy, *British Economic Policy, 1945-50*, London and Cambridge Economic Service, May 1950, p. 5.

<sup>26</sup> W. A. Lewis, Britain's Survival Depends on Flexibility, *Economic Digest*, Jan. 1951, p. 6.

<sup>27</sup> Cf. *ibid.* and Graham Hutton, The Planned Neglect of Capital Formation, *The Banker*, XCV, 294, July 1950.

<sup>28</sup> *Economic Survey for 1947*, *op. cit.*, p. 25.

<sup>29</sup> Capital Investment in 1948, *op. cit.*, p. 12.

the economy became more viable, more long term investment became feasible. For foreign trade, there was continued need for rapid returns.

In applying its criteria, the IPC knew it had to tread carefully. The 1951-53 defense program which required both direct investment and, for increased output, scarce resources as steel which could otherwise be used for investment, was originally a given figure. The IPC could not propose cuts, though it might advocate shifts of the three year total between the years. Housing was another sensitive political field due to enormous public demands. The IPC could not advocate cuts in the program, though it might point out to Ministers the implications—i.e. more homes mean fewer factories. But without instructions from Ministers it could not proceed on investment allocations on the assumption of a lower housing program. On the other hand, it did advocate cuts in less sensitive fields, such as health and education for 1951. On the whole, the IPC took into account specific instructions, broad directives, general criteria and "political atmosphere" in framing investment programs.

Following its deliberations, the IPC printed a report including original programs presented by Departments and its recommendations on total investment and sectoral allocation. These had to have approval of the Chancellor of the Exchequer, who had been in frequent contact with the IPC throughout. His personal strength of character, his economic knowledge, his interest and forcefulness determined the extent to which his influence limited the IPC's autonomy. Both Cripps and Gaitskell did exert influence.

For 1951, maximum and minimum alternatives were presented. The maximum was subsequently adopted by the Ministers. Ministerial decisions were based largely on the figures and much of the reasoning in this report. Once framed, the program was difficult to alter. The IPC had conducted lengthy hearings. Its members were the only ones who had considered all the different programs presented in detail. Its recommendations had the Chancellor's approval. As a result these recommendations were not altered much. Naturally some Ministers felt frustrated when faced by this.<sup>20</sup>

<sup>20</sup> The considerable potentiality for power of a strong Chancellor is clear.

The IPC program was first considered by the Economic Steering Committee which included Permanent Secretaries of Departments. It was large, unwieldy, full of extremely busy men, lacked background information. In practice it changed nothing, though general comments might be made. This Committee recommended the report as a whole to the Ministers, though Departments could make reservations of disagreement to be pursued to higher levels. This was infrequent, for each had already argued before the IPC and sustained cuts like others. It knew that other Ministries could also make reservations whose sum total would amount to restatement of original programs.

An outside committee, the Economic Planning Board, composed of representatives of the principal employers' organizations, the Trades Union Congress, economic Departments, Economic Section of the Cabinet Offices and Central Economic Planning Staff (whose head was usually chairman), was set up in an advisory capacity (1947) to keep labor and management in touch with government and economic planning. Its members were shown the IPC report and made suggestions. They did exercise some influence. This committee was just part of continual consultation between Departments on the one hand and business and labor on the other. These latter accepted physical controls to prevent chaotic scrambles. In return their support was needed for smooth administration of controls.

Then the report went to the Production Committee of the Cabinet which included the Chancellor of the Exchequer as chairman and the economic Ministers such as the President of the Board of Trade and the Ministers of Supply, Fuel and Power, Transport and Works. In case of disagreements individual Ministers could appeal upward for they were not bound by the committee's decisions. The Chancellor's influence diminished disagreements.

Now came the Economic Policy Committee of the Cabinet, chaired by the Prime Minister. Membership included the Chancellor, Foreign Minister and Lord President of the Council. From it there could be appeals to the Cabinet itself with the Prime Minister as final arbiter.

The approved report was distributed to high civil servants

and applied, subject to revisions in case of major changes in economic situation.

#### BOTTLENECK PLANNING

*Planning and Economic Conditions:* Content and methods of investment programming changed with changing circumstance. Planning had to be flexible to overcome different obstacles as they arose to hinder attainment of objectives. "The programmes for capital development are under continuous adjustment and revision."<sup>31</sup> Sir E. Bridges, Permanent Secretary of the Treasury, had this to say.

I do not suggest that there is any finality about the instruments or methods of analysis at present used in the direction of our economic policy. The methods now in use have been developed to meet the conditions of the last five years, and as those conditions change so will the methods in use.<sup>32</sup>

Investment planning revolved about the "bottleneck" factor which either limited investment of certain types or investment as a whole. These bottlenecks changed. In the immediate postwar period, before advent of effective investment programming, there were many intertwining bottlenecks of specific labor shortages (in building, coal, textiles, agriculture) and lack of materials (e.g. timber), some of which in turn were related to the balance of payments "bottleneck." Shortages continued in 1947 as production expanded; the coal crisis came in February '47, the foreign exchange crisis in August and then establishment of the Central Economic Planning Staff.

The 1948 investment program, drawn up late '47, projected investment cuts to release labor and materials for export production and largely hinged on steel as a limiting factor. Timber, raw materials as sulphuric acid, caustic soda and soda ash, as well as labor in coal, textiles, agriculture were expected to provide further limits on investment, production and exports. The foreign currency shortage, a bottleneck of a broader type, prevented purchases abroad or releases from export production to home use which might have softened some bottlenecks.<sup>33</sup>

<sup>31</sup> *Economic Survey for 1948, op. cit.*, p. 39.

<sup>32</sup> Sir Edward Bridges, Permanent Secretary to HM Treasury, *Treasury Control* (Stamp Memorial Lecture 1950), p. 24.

<sup>33</sup> *Economic Survey for 1948, op. cit.*, passim.

The 1949 investment program, formulated in '48, was limited by steel and timber shortage, both derived to an extent from foreign currency shortage. This in turn was influenced by labor shortages in textiles and coal hindering exports. Non-ferrous metals and some other materials provided limits in specific products.<sup>34</sup>

The 1950 investment program total, drawn up in 1949, no longer pivoted on steel shortage. All steel except sheet and tinplate came off allocation May '50. An over-all savings-investment balance was drawn spring of '49, since consumption which the community was willing to forego, coupled with needed exports, was considered the main limiting factor for 1950. Then, the September '49 devaluation made it imperative to curtail creation of purchasing power to prevent inflation. The 1950 investment program was cut at the end of '49. Besides the over-all limit there were some specific shortages such as timber which depended on foreign currency availabilities and labor in coal mining which limited coal exports, a factor in the balance of payments difficulties.<sup>35</sup>

In the spring of 1950, detailed savings-investment figures were drawn up on Gaitskell's instructions. The 1951 investment program, formulated before June '50, conceived of the community's willingness to save as the main factor limiting investment, though some specific shortages as sheet steel, tinplate and probably timber would continue. Labor shortage in coal would again limit coal exports.<sup>36</sup> Many bottlenecks had disappeared. "If one considers the bottlenecks (coal, steel, timber, electricity) collectively, they are clearly very much less potent than they were a few years back."<sup>37</sup>

After Korea, shortages reappeared. Materials became more difficult to secure. Demands for defense investment and production increased. The 1951 investment program was revised. Cuts were made in education and health. New office buildings, entertainment places, blitzed-area reconstruction were drastically diminished. Defense projects increased. In 1951 there were shortages of sulphur, non-ferrous metals and progressive tightening in steel causing reintroduction of allocation at the

<sup>34</sup> *Economic Survey for 1949, op. cit.*, passim.

<sup>35</sup> *Economic Survey for 1950, op. cit.*, passim.

<sup>36</sup> *Economic Survey for 1951* (Cmd. 8195), passim.

<sup>37</sup> E. A. G. Robinson and A. D. Roy, *op. cit.*, p. 3.



end of the year. Steel production was cut by lack of sufficient iron ore imports due to shortage in shipping space which had been used for coal transport, as well as a drop in German scrap supply. The 1952 investment program was again formulated largely on specific bottlenecks, not over-all limitations.

*Scope of the Investment Controls:* Central planning of investment through physical controls was negative in character. No one was forced to do anything. Many were prevented from doing something.<sup>38</sup> The usefulness of restriction depended upon surfeit of demand for investment as during this period. By deciding which projects were to get preference, the government determined in which direction, out of many desired directions, progress was to be made first. It did this only to the extent of providing permission for investment where demand for investment already existed. It allocated investment among competing demands for those types where demand exceeded supply. The less specific the bottleneck, the less the control of investment planning. When specific bottlenecks disappeared, physical investment controls became tenuous.

What central investment planning did not do was to create demand for investment. Physical controls over basic materials and building licenses did not determine demand directly. They could only decide between competing existing demands. But central investment control did have indirect effect on demand for investment. First, to the extent that it limited investment, it influenced one of the determinants of the general level of activity which affects demand for investment in the private sector as elsewhere. Second, by choosing the sector (out of many desired) in which rate of growth was to be greatest, it could stimulate further demand for products undergoing rapid technological improvements and cheapening.<sup>39</sup> This in turn could cause more demand for investment in that sector.

The demand for investment was exerted through private industry, public industry, government and individuals directly.

(a) private industry: Demand for investment was affected by expectations on the general level of economic activity,

<sup>38</sup> But those who were prevented from doing one thing might be forced to do something else. Denial of permission to construct a new factory elsewhere forced a manufacturer to locate in a Development Area or not build at all.

<sup>39</sup> I.e. the effect of production on demand.



distribution of incomes, income taxes, business taxes, purchase taxes, subsidies direct and indirect, price controls, export demands, etc. and the interest rate and costs of investment. The government influenced demand for investment by business only indirectly through fiscal policy, monetary policy, and price controls. This indirectness did two things. First, since business demand for investment depended on expected profits, controls were limited to those which did not remove too much profit incentive. This reflected back on income distribution which determined whether the ultimate demand for investment was (ethically) "correct." Second, it produced conflicts. Simultaneously, demand for investment was cut through central investment controls and stimulated elsewhere. Until the 1951 Budget, initial depreciation allowances were kept high to encourage investment demand for industrial modernization. This fostered demand for machinery and buildings to house it, non-selective as between industries. More selective were certain subsidies to increase reequipment in the textile industry. Development Councils, which might make compulsory levies for research on firms in specific industries, also could stimulate some reequipment.

On the whole, control over the rate of progress in the private sector was very limited. For example, the government predicted a sulphur shortage. It attempted to persuade manufacturers to install plant to process sulphuric acid from iron pyrites or the anhydride by a more expensive method than production from sulphur. Manufacturers declined; they did not foresee shortage and were unwilling to utilize less profitable methods. By the end of 1950 a sulphur crisis was at hand. The government had only been able to promise building licenses if manufacturers would construct new plants. New plants could not be forced. The controls were permissive, not compulsive.

(b) public industry: In theory, the government exercised complete control over demand for investment by nationalized industries. In practice, it did not. Nationalized industries were "autonomous" to a large extent. Demand for investment of nationalized electricity and transport, though not coal, tended to exceed potential supply of available resources, so that demand stimulation was not a problem in these two cases.

(c) government: It controlled its own demands for invest-

ment. It also exerted telling influence over investment demands which depended on Exchequer grants.

(d) individuals: Direct private demand for investment, largely small housing repairs and some housing, was only influenced indirectly by controls over prices, incomes and interest rate.

*Planning on Bottlenecks:* Britain's central investment planning in the sense of "directionalizing" investment was only effective when there were specific bottlenecks which could be administratively attacked.

A bottleneck exists when demand exceeds supply for a specific price. It may not be possible to equate demand and supply for two reasons. First, there might be adverse social effects. Second, required price changes may be large. (a) When mobility is limited and friction considerable, even large price increases may not draw enough resources into crucial sectors. (b) Large price increases may not suffice to decrease amount demanded sufficiently. (c) When there are fluctuations in quantity of a material available (e.g. sulphuric acid) large price fluctuations are likely. Price rises and price fluctuations can impel inflation, disturb production and exercise unstabilizing influence.<sup>40</sup>

Bottlenecks can only be eliminated by shifting resources. But many resources are specific and many immobile. If all input mixes (including labor and plant) could instantly be turned to produce any output, there could be no specific bottlenecks, though a general savings—investment "bottleneck" might remain. In practice, factor substitutions are limited; adaptation takes time; shortages of labor, raw materials, and plant persist. Speed of bottleneck elimination depends on factor mobility and substitutability. Both were limited in Britain. Labor shifted jobs slowly. Acquisition of new skills took time. Management was less adaptable than American. Lack of standardization prevented interchangeability.

Bottlenecks also depend on the size of stocks. The smaller are stocks and the less mobility, the greater danger of simultaneous bottlenecks with different limiting factors, which would not exist were there perfect distribution. In an "empty econ-

<sup>40</sup> Unstabilizing expectations are created.

omy," one plant can end with too much coal and too little iron ore, another with too much iron ore and too little coal.

Planning seeks to eliminate bottlenecks holding up production, though other potential bottlenecks may hover in the background. It is clearest in war.

The principle was laid down that production had to be estimated on the basis of the narrowest bottleneck. For instance, equipment and raw materials might be ample, but if it was coal or labour that was in short supply, it was in accordance with *these* that plans had to be drawn up. As bottlenecks were constantly shifting, the basis of the plan had constantly to be altered. The real art of this part of central planning lay in recognizing promptly where the bottleneck was to be expected next.<sup>41</sup>

Resolution of bottlenecks involved decisions on relative importance of different interconnecting bottlenecks as well as choice between alleviating present difficulties or those likely to appear in the future. Should there be dollar exports immediately or expansion of basic industries? It takes steel to produce steel. Was it to be used for construction of steel plants, for factories, for exports directly or incorporated in machinery? Needed was a model of the economy (and some foreign demands and supplies) to pursue the effect of alternate policies into the future. Statistics were not (usefully) available. Theory was being developed.

When, after five years of planning it was recently (1950) decided to set up the rudiments of a model (of the economy, effects of different taxes, etc.) . . . the increased facility with which subsequent reports were produced was surprising.<sup>42</sup>

There were two effective limits to British central investment planning with supporting controls. If (1) a non-attackable bottleneck appeared or (2) specific bottlenecks disappeared it became ineffective.

(1) The main bottlenecks which could not be administratively attacked involved labor. Control over labor movement was very limited. There were incentives, e.g. higher wages, for

<sup>41</sup> Walter Eucken, On the Theory of the Centrally Administered Economy: An Analysis of the German Experiment, *Economica*, XV, 58, May 1948, p. 83.

<sup>42</sup> Marris, *op. cit.*

some jobs, disincentives for others; there was some "guidance" through placement of job applicants by Labour Exchanges; no direct controls were usable. Bottlenecks persisted in some fields. During part of the postwar period textile exports were limited by textile labor. Coal was a crucial case. More coal miners produce more coal. More British coal would have meant less Western European coal imports for scarce dollars. Elimination of the transatlantic haul would have released shipping space. In the winter of 1950-51 shipping shortages reduced iron ore imports into the U.K. and steel production.<sup>43</sup> Coal exports would also have improved the foreign balance and secured vital imports in return. Clearly coal labor shortage was central in British bottlenecks.<sup>44</sup>

To a limited extent, the foreign balance could be considered a non-attackable "bottleneck." Foreign demand and relative rises in import prices were largely beyond administrative control. This was a broad, general "bottleneck" whose import components could be manipulated. But in case of absolute shortage of a foreign raw material, a serious specific bottleneck could arise.

(2) When specific bottlenecks disappeared British investment controls tended to become ineffective.

First, "directionalization" of investment, in the sense of choosing which of several demanded investment projects was to proceed, ceased.

Second, we have seen that central investment planning was not designed to stimulate demand for investment directly. It could not increase investment in any sector of the private economy when business did not wish to invest (e.g. sulphuric acid).

Third, without specific material bottlenecks, regardless of an over-all savings-investment limit for the economy, immobility of resources made it difficult for British physical investment controls to decrease investment involving a material not in shortage. With "immobile" resources, a cut in a type of investment not limited by material shortages tends to free resources

<sup>43</sup> The factor limiting ore imports might be considered alternatively either (a) need for coal imports into Europe or (b) insufficient shipping space.

<sup>44</sup> This illustrates a difference between war and peace. In the war, the "Bevin Boys" were drafted into coal mines instead of the army. In peace, such direction of labor was not feasible.

which go idle for a time. A completely immobile resource, to be sure, has no marginal cost. But "immobility" is *Relative to Effectiveness of Controls* designed to shift resources to other uses. In Britain controls were often modified by resource immobilities rather than resource immobilities by controls. Immobility rather than national policy became a guide; planning abdicated to expediency. When building labor was left idle by building investment cuts designed to release it for other tasks, it sought to eliminate the cuts (e.g. 1948).

Due to these limitations<sup>45</sup> change in conception and techniques of planning seemed imminent prior to Korea. In early 1950, considering potential exports as modified by German and Japanese competition and investment the home market could take without serious inflation, it was thought further engineering industry expansion might have to be prevented. But without specific shortages investment controls could not do so. The Swedish idea of taxing capital investments during inflationary periods was considered. This could be made selective by differentiation by broad industry groups,<sup>46</sup> regaining some control over investment through indirect methods, though selectivity of such a system is good only to the extent that expected profits<sup>47</sup> are good indicators of investment needs. Then Korea reintroduced specific shortages. Central economic planning depending on shortages could be resumed.

*Other Limitations:* (1) Removal of controls: As bottlenecks were eliminated so were controls.

Direct controls are being progressively removed, although the planning authorities are having difficulty in keeping private investment down to the level set by the available resources left over from personal consumption and the present use of goods and services in the public sector.<sup>48</sup>

During 1945-50, factory space was decontrolled, direction of labor removed, general purpose steel and some raw materials

<sup>45</sup> One limited function remains for planning. Even without shortages and desire to increase or decrease investment in any sector, physical controls might be conceived as substitute distributing mechanism for an inefficient market. This was not the rationale behind British controls.

<sup>46</sup> Differentiation could certainly not have been carried to individual firms.

<sup>47</sup> On the (taxed) investment, cf. above.

<sup>48</sup> Government Spending, *Political and Economic Planning (PEP)*, XVII, 317, Aug. 21, 1950, p. 21.

taken off allocation, timber restrictions loosened, coal miners permitted to enter other industries, building license repair limits raised, import controls relaxed. We have seen that such controls were of limited use without specific bottlenecks. This also lapsed with their repeal. After shortages due to rearmament some controls reappeared. Steel and sulphur were put under allocation, end uses prohibited for some non-ferrous metals, e.g. copper and zinc.

(2) Investment in machinery: There was no direct control. Already in December 1947,

Unlike investment in building, investment in plant and machinery is, with few exceptions, now free of direct controls. Decisions as to the level of investment in plant and machinery are, therefore, less certain and direct than in the case of buildings.<sup>49</sup>

Wartime machinery licensing was dropped due to difficulties in deciding on allocation of individual machines and administrative staff necessary. Indirect controls remained. Building licenses for structures to house machinery additions were only granted to "essential" firms, but few firms needed new buildings at any one time. Import licenses for machinery went to "essential" firms, but imports were not high. Export stimulation persuaded many firms to export, leaving less machinery in Britain. Steel allocation could be used to urge manufacturers to sell to essential users. The 1951 cut in initial depreciation allowances discouraged investment in machinery.

Each year, the IPC compared expected machinery demands with potential supply. But it could not allocate limited supply to users. Larger firms planned further ahead, ordered sooner and usually got more of requirements. In practice, any firm desperately in need of equipment appealed for aid to its Government Department. If the firm had been "good" (i.e. had high exports, etc.), the Department contacted its counterpart in charge of machinery manufacturers which persuaded one to supply equipment. These "household functions" of government were extensive.<sup>50</sup>

<sup>49</sup> Capital Investment in 1948, *op. cit.*, p. 6.

<sup>50</sup> Cf. Pigou, Central Planning and Professor Robbins, *Economica*, XV, 57, Feb. 1948, p. 21—"The Government is in the position of a chess player, some of whose most important pieces are not subject to his will, but are free to make moves of their own volition."



(3) Investment in stocks: There was no direct control besides imports controls and allocation schemes for certain materials.

(4) Building repairs: There was no control over building repair and maintenance beneath the license limit.

An accurate estimate of the total expenditure on repairs, maintenance and conversion of existing houses is not possible since much of the work does not require a licence and is generally undertaken by small firms of private builders on behalf of private individuals.<sup>51</sup>

If not possible to estimate, it was certainly not possible to control. The sum total was not negligible. In 1950, repair expenditure on buildings and works was £697 million, compared with £585 million outlay on buildings and works proper out of total fixed capital formation of £2162 million. Unlicensed repairs were running about £200-250 million annually. The license limit could be lowered, but not too much without great administrative efforts.

(5) Statistics: Adequate planning requires a model of the economy. Input-output and capital-output matrices with marginal transformation ratios are necessary for better estimation of results of investment allocation, while demand analysis must gauge consumer preferences. Further, some criteria have to be set up to deal with time preferences. The necessary data, particularly the marginal capital-output ratios, were often not available. Planners had difficulty in analyzing the results of possible decisions. "The greatest part of the difficulty lies in assembling and analyzing the data and the speed with which it is usually necessary to take decisions."<sup>52</sup>

(6) Momentum of the economy: An economy is not pliable like putty.

Since capital projects take many years to carry out, changes cannot be made at short notice, without disproportionate waste and dislocation, and programmes are now therefore planned for several years ahead.<sup>53</sup>

Zone of choice in allocating investment is limited by the

<sup>51</sup> *Economic Survey for 1950, op. cit.*, pp. 47-48.

<sup>52</sup> *Marris, op. cit.*

<sup>53</sup> *Bridges, op. cit.*, p. 23.



state of the economy and strength of the controls.<sup>54</sup> Investment allocation must take into consideration the size of existing capital stock of each type, need for repairs, and necessity for "balanced development" through time for new investment. Allocations have to be granted to projects already begun. "The controls cannot by themselves bring about very rapid change or make very fine adjustments in the economic structure."<sup>55</sup> Possible adjustments are marginal; if attempted to excess, immobile resources are wasted.<sup>56</sup> Resources can be wasted permanently or through lack of complementarity due to bad timing. Planning seeks to avoid both.

Adaptability to short term crises was limited. Korea could not induce investment shifts to defense overnight. Materials, labor, plant had limited mobility. Conversely, cuts made due to crises which later turned out of short duration could not be restored at will. The 1950 electricity program was less than expected partly for this reason. The nature of controls limited rapidity of adjustments. When building license issue was reduced the immediate result was construction of fewer buildings more rapidly; there was a time lag before investment declined.

#### SUCCESS OF INVESTMENT CONTROLS

British central investment allocation was restricted by all the limitations cited previously. Most notably, it failed whenever decreases in investment were planned, especially when labor immobilities were involved.

The clearest example was 1948. The *Capital Investment for 1948* White Paper of December 1947 projected considerable investment reductions. Foreign exchange crisis in August 1947 made it imperative to release resources for exports. Actually, investment failed to decline. Gross domestic capital formation rose from £1,835 million in '47 to £2,120 million in '48. The *Economic Survey for 1949* explained this large deviation from plan,

In the event, the receipt of ERP aid and the increase in steel output, made it possible for a less restrictive policy to be followed, and investment in 1948 proved to be substantially greater than in 1947.<sup>57</sup>

<sup>54</sup> The more effective controls, the less "immobility of resources," within limits.

<sup>55</sup> *Economic Survey for 1947*, *op. cit.*, p. 8.

<sup>56</sup> Power of adjustment depended to a noticeable degree on strength of controls.

<sup>57</sup> *Economic Survey for 1949*, *op. cit.*, pp. 3, 4.

That the investment program had been based on hypotheses of the national economic position which later turned out unduly pessimistic is true. (This itself was failure in prediction.) It was expected that "real levels of consumption in 1948 will be appreciably, but not disastrously, lower than in 1947."<sup>58</sup> In the event, real personal expenditure on consumers goods and services increased slightly. But improvement in economic position could not justify all the investment increase. It was not held back according to (modified) policy.

Building construction was supposed to decrease perceptibly. Actually, expenditures on buildings, works and repairs increased some 30 per cent. In July and November lower limits for unlicensed repairs were raised, making building repairs easier. Improved conditions partly explained this almost 50 per cent deviation from planned expenditures. Much more important was failure to push excess building and civil engineering manpower into other sectors. The manpower target for end of 1948 in the *Economic Survey* was 1,200,000 men. The actual end of 1948 figure was 1,357,000, almost no decline from 1,364,000 at the end of 1947 which was substantially ahead of the end of 1947 target and at that time "larger than the present supplies of materials can sustain."<sup>59</sup> Building labor failed to move to more essential occupations. Increase in building license issue and rise in lower limits for unlicensed repairs depended on need to keep labor force employed. Planning followed an immobility rather than effectively removing it. Increase in investment in machinery, plant and cars in industrial use, on the other hand, was due to iron and steel production increase which permitted policy modification, not to failure in controls.

In 1949, no such great changes in investment were planned. Total investment in the main sectors did not differ greatly from forecast.

The 1950 program, following devaluation September 1949, planned a very small decrease of gross fixed investment (at end of 1949 prices) in the principal sectors. In the event, there was about a 4 per cent increase.

The increase of £80 million was partly due to price changes, and

<sup>58</sup> *Economic Survey for 1948, op. cit.*, p. 53.

<sup>59</sup> *Ibid.*, pp. 42, 43.

there was only a small increase in the physical volume of investment in 1950. This fact may be attributed mainly to the restrictions imposed on investment after the devaluation of Sterling in Sept. 1949, although it later proved possible to relax these restrictions somewhat as a result of the general improvement in the economic situation.<sup>60</sup>

Restrictions were more effective in this case. The building license repair limit, for example, was reduced February 1950. But gross fixed investment in housing (including repair and maintenance) which was to drop some 5 per cent, remained about the same. Labor in building and contracting industry again exceeded (end of 1950) targets. Decreases in transport and communications investment were less than projected. On the whole, there was no wide deviation between plan and actuality, largely because no great changes had been planned in the first place.<sup>61</sup> Labor immobilities again proved intractable.

For 1951, no investment program was published due to defense program changes and uncertainties. Manpower targets also were missing. This was probably due to the fact that investment program figures would not have been likely to correspond closely to actuality under 1951 conditions. There were revisions of investment allocations for 1951 well into 1951. The original 1951 program was prepared the first quarter of 1950. In August 1950 there were special revisions due to defense expenditure increases following Korea. Further revisions came in January 1951 due to further expenditure increases. In fact, the year was so exceptional that some sectors did not receive final 1951 investment allocation (cuts) until June 1951. Investment cuts at such late date could not be realized. Time was needed to revise programs.

#### CONCLUSION

British investment planning was carried out against a background of (1) national crisis and (2) demand for social welfare. Two themes were central, (a) the balance of payments problem and (b) a period of excess demand, the former shaping the objectives of planning, the latter the methods.

The efficacy of investment controls was limited by their extent and power. The controls modified many resource

<sup>60</sup> *Economic Survey for 1951, op. cit.*, p. 23.

<sup>61</sup> Possibly because they would not have been secured.

immobilities; but often they adapted to immobility rather than removing it. Investment controls could produce only marginal changes, though "marginal" is partly defined in terms of the potency of controls. Changes had to be planned long in advance to be effective and the economy had to undergo "balanced development." Controls changed as bottlenecks changed. They tended to atrophy in step with disappearance of bottlenecks.

Britain's physical controls over investment influenced not the demand for investment but the distribution of available supply of investment resources. They were limited to restriction and effective only as long as shortages and bottlenecks persisted. When an intractable bottleneck appeared and could not be administratively attacked (e.g. labor), physical investment controls became nugatory.

The investment controls succeeded in channeling some investment to crucial sectors, in eliminating much unnecessary investment, in preventing wasteful use of materials. But their power over many types of investment was small. On the whole, investment controls were partly controls and partly mere indicators of events, partly in the position of driver and partly in that of speedometer. On the one hand, the investment planners were quite powerful within their limited framework of controls; on the other, what this sort of planning was able to do was restricted. It was effective only during periods of excess demand and then in limited fashion.

## DIMENSIONS OF PLANNING

Y. Dror

THIS paper is devoted to an analytical examination of the meanings and components of "planning." Through systematic construction of a framework of concepts, which are put into relation as parts of a model of planning, an attempt is made to focus attention on some problems which are implied in planning as such, and to provide some of the necessary conceptual tools for dealing with them.<sup>1</sup>

Because of the complexity of the issues, no attempt can be made here to cover all of them; nor is it the main objective of this paper to provide a definitive new terminology for dealing with concrete planning problems. It is rather in the hope of showing the potential usefulness of analytical examination as a device to distinguish between verbal difficulties and really significant issues in the field of social planning that this paper is written.

### THE MEANING OF PLANNING

This paper being devoted to "planning," we might well start, by trying to define this elusive term. This is made all the more necessary, and difficult, by the oversupply of definitions of planning offered in the infinite professional, quasi-professional and semi-professional literature on this subject.<sup>2</sup> If we take the totality of human action as our field of discourse,<sup>3</sup> and keep in mind the purposes of this paper, it seems to the author that the most useful definition of planning is "*action-oriented thought*."<sup>4</sup>

<sup>1</sup> This paper tries to apply to planning an approach which is receiving growing recognition within the social sciences. This approach incorporates the advances made in semantics and analytical philosophy and tries to apply them to the social sciences, endeavoring to construct conceptual frameworks and models which can be used for systematic classifications and thorough analysis of various social facts and problems. It would lead us too far to discuss here the general theoretical justifications and practical importance of this method. Cf. Israel Scheffler: "Toward an Analytical Philosophy of Education," 24 *Harvard Educational Review* 223, 1954.

<sup>2</sup> For a collection of some of the more important definitions, see John D. Millett: *The Process and Organization of Government Planning* (1947), p. 2 *et seq.*

<sup>3</sup> On the dependency of definitions on limited worlds of discourse, see Ogden and Richards: *The Meaning of Meaning* (1947), Chapter VI. The almost complete lack of uniformity in the use of the verbal symbol "planning" seems to be due to a considerable extent to the diversity of aims and contexts within which it is used.

<sup>4</sup> Cf. F. A. Hayek: *The Road to Serfdom* (1944), p. 26.

This is a rather wide definition, which includes within its scope planning on the individual as well as on the institutional level. In order to clarify its meaning, it is necessary to elaborate somewhat the distinction between "action-oriented thought" and other forms of activity. This we shall do by examining some inter-related propositions.

1. Human activity includes thought and action. While there are additional elements to human activity (e.g., "feeling," "dreaming" etc.) and while it is not easy to define "thought" and "action," the analytical distinction between them seems clear enough to warrant reliance on it for our purposes. It is possible to imagine "action" without a significant degree of "thought," e.g., ritual action, reflective action. On the other hand, though it may be that thought is always accompanied by certain physical processes in the nervous system, and systematic thought is often helped by and dependent on secondary action (e.g., writing outlines, drawing graphs, etc.)—thought can analytically be distinguished from action.<sup>5</sup>

2. Thought can be oriented towards various classes of objects, such as pure problems (in mathematics and in pure science), values, action and so on. By definitions, we refer by planning to action-oriented thought. Other categories of thought may be relevant to planning, e.g., pure research may be essential for providing the knowledge needed for effective planning, but must be distinguished from planning itself.

3. Propositions one and two deal with processes on the level of the individual. By analogy, the distinction between "thought" and "action," and between thought oriented towards various objectives and purposes, can be applied to the institutional level. This does not imply any organic conception of society and social institutions, but recognizes the analytical difference between "considering" and "executing" functions, and the possibility of classifying institutions according to the predominance of either of these functions.<sup>6</sup>

<sup>5</sup> This was not denied even by the behaviorists, whose claim it was that thought as such cannot be subjected to scientific investigation.

<sup>6</sup> From the methodological point of view, we have here two pure types: Institutions which are only considering, and institutions which are only executing. "The question is always one of more or less, or one of defining the position of a concrete phenomenon upon a scale of infinite transition between two extremes of clear-cut polarity." (Max Weber on Law in *Economy and Society*, Introduction by Max Rheinstein (1954) p. XXXVI.) To some extent, this distinction points to

On the institutional level, the distinction between the *planning function* and a *planning institution* is of special, fundamental importance and must be kept in mind. A planning institution is a social unit which engages primarily in planning, but it may engage in various additional functions, such as promotion, plan-execution and so on. On the other hand, the planning function is pervasive; every social unit engages to some extent in planning. Failure to keep in mind the distinction between planning as a function and planning institutions has contributed greatly to unclear thinking.<sup>7</sup>

Up to now, we have tried to define "planning" and to show some of the implications of our definition. The implications of planning, defined as "action-oriented thought," both on the individual and on the institutional level, have been discussed and the distinction between planning as a function and planning institutions has been emphasized.<sup>8</sup>

We are now ready to proceed to an examination of some of the dimensions of planning, but it may be worth while to re-examine first, in the light of our definition, some of the problems concerning the desirability and possibilities of planning.

#### DESIRABILITY AND POSSIBILITIES OF PLANNING

It is easy to conceive of differences of opinion on *planning conclusions*, i.e., *the conclusions as to desirable action (or non-action) reached through planning*; different persons and different institutions can reasonably hold different opinions as to what the best course of action should be. But, *prima facie*, it seems that there should be no difficulty about accepting the method of

some aspects of the "staff" and "line" dichotomy, accepted in public administration.

<sup>7</sup> Note the inconsistencies in the use of the concept "planning" in the book by Robert A. Walker: *The Planning Function in Urban Government* (1950), which seem to be caused largely by lack of attention to this distinction.

<sup>8</sup> From a systematic point of view it would be desirable at this stage to proceed from the analytical distinction between planning and other activities to an examination of the structural differences between the units fulfilling planning and other functions. But neither the study of the human brain nor the sociology of bureaucracy are sufficiently advanced to permit any such investigation on the individual or the institutional level. For a pioneering book which does shed some light on the structural aspects of planning on the institutional level, see Herbert Simon: *Administrative Behavior* (1947). It seems that there are differences in the processes of selective communication between bureaucratic structures engaged mainly in planning and bureaucratic structures engaging mainly in research, action or other types of activity.



dealing with our problems rationally, by thinking about them, i.e., by planning. But matters are not as simple as that. Opposition to planning can be supported by two lines of arguments: One argument, while admitting the theoretical desirability of planning in the abstract, denies that it is possible, or at least confines its feasibility to narrow borders. The second argument denies the desirability of planning *per se*, even if it should be feasible.

Let us take up the second argument first. It is based either on the belief that certain subjects should not be thought about because of their inherent character (taboo), or on the feeling that planning constitutes a prohibited interference with the ordained order. This line of argument has considerable weight in many of the underdeveloped countries, slowing down their development, but we should recognize that it is also part of the values of Western Culture, though it is limited to certain fields. E.g., institutional planning of selection of mates for marriage is rigorously rejected in our society, mainly because of ideological reasons. A somewhat different basis for the argument, which to some extent is accepted in all contemporary societies, concerns itself with the segregation between individual and social spheres of action. Institutional planning is excluded from certain areas, which are left to the activities, including planning, of the individual. While the borderline between these two spheres is an elastic one, there are always limits beyond which institutional planning is not permitted to go.<sup>9</sup>

Assuming the desirability of planning *per se*, we are still faced by the first argument: To what extent is planning possible? Let us examine the meaning of this question. The problem is mainly one of feasibility and worthwhileness: The significant question is if, and to what extent, do the possible results of planning justify the necessary investment of resources. In order to answer this problem, at least two factors must be con-

<sup>9</sup> One must keep separate the allocation of spheres of activity to individuals as a conclusion of planning, and the *a priori* exclusion of institutional planning from certain areas. E.g., most contemporary exponents of laissez faire justify their conclusion in terms of rational economic arguments. They want to limit state interference with the economy because this, in their opinion, is the most rational way to arrange the economy. Here, non-action is the conclusion of planning. On the other hand, the same conclusion can be reached on the basis of "natural law," "rights of the individual," or some other value-basis.

sidered: The resources available for planning, and the results of planning, as compared with the results of non-planning.

Let us start with the individual. At any given moment the quantitatively and qualitatively limited capacity of the human mind is the absolute limit on the resources available for planning.<sup>10</sup> Another limit is the necessity to devote a minimum of resources to life-sustaining activities: sleep, eating, etc. The resources available after these minimum requirements are satisfied, will have to be allocated to various activities, including planning. The most economic allocation would insure maximum over-all satisfaction in terms of the individual's value-system.

Similarly, on the institutional level, the available resources (including man-power with varying capacities, knowledge, physical resources and so on) are definitely limited at any point in time, and the necessity of allocation between competing activities, and within the planning activity, between different fields of planning, has to be faced. The optimum solution of this problem will depend on the marginal utility of the available resources when devoted to various activities. This, in turn, depends on the utility of planning: the results of planning as compared with the results of non-planning.

Planning is action-oriented thought, i.e., thought which is directed at reaching conclusions in regard to desirable courses of action. The effectiveness of planning depends on its success in providing successful courses of action. Every action can have four classes of results: (a) expected and desired; (b) expected and undesired; (c) unexpected and desired; (d) unexpected and undesired. Successful action should result in a preponderance of desired over undesired results, but this alone is not sufficient to justify the investment of limited resources in a certain activity: it is necessary that the net, desired results of the activity, as compared with the results of non-activity, should represent the best possible use of the resources. In other words, available resources must be allocated between various activities in such a way as to assure the maximum total desirable result. Or, the marginal addition of desirable results per unit of resources must be equal for all fields of activity.

<sup>10</sup> This limit may be either permanent or temporal, i.e., changeable through education, experience etc.

This abstract analysis shows some of the factors to be taken into account when discussing the possibility and worthwhileness of planning. It is possible to elaborate further this abstract model but no useful purpose would be served by this. Rather, it is necessary to draw attention to the difficulties of applying this abstract model to concrete issues: It is almost impossible to predict the conclusions of planning and the results of plan-execution; the allocating body rarely tries, or is able, to allocate resources on a scientific basis;<sup>11</sup> in any case, "desirability" is a matter of value judgment. Even on the individual level no full integration of desires is ever achieved. On the social level, consensus rarely goes beyond very general symbols and values, which are nearly valueless as a guide for planning and a measuring-stick for plan-execution.<sup>12</sup>

These concrete difficulties do not impair the theoretical validity of the abstract analysis and its practical value as an ideal which should be realized as far as possible. In all concrete cases all the relevant factors mentioned have to be examined and evaluated, as far as is humanly possible, if a rational answer is desired to the question of "worthwhileness" of planning in a certain instance.

To sum up: Opposition in principle to planning is related to certain values and ideologies, including fundamental beliefs on the nature of the world, individuals and society. After overcoming basic ideological opposition to planning, as such, the problem of feasibility and worthwhileness of planning must be faced. The quantitatively and qualitatively limited resources must be allocated in the best possible way between competing activities and, within planning, between different field of planning. The subjective character of all evaluative judgments and differences in values make it nearly impossible to apply to concrete social problems the abstract formulas yielding in

<sup>11</sup> The haphazard manner of budget-making by nearly all national legislatures is regarded by many planners as one of the best illustrations of irrational allocation of resources. One of the first efforts of many planners is directed at assuring more rational allocation of money between various activities and the exclusion of irrational action from this field. Cf. the section dealing with budgeting in the Planning Law of Puerto Rico (Act 213 of 1942) and the parallel provisions of the New York City Charter.

<sup>12</sup> It is interesting to observe that systematic public support for large-scale and intensive planning and plan-execution is generally limited to subject-matters in regard to which there is general consensus on an acute need for interference; e.g., periods of economic crisis or war, depressed areas, floods etc.

theory the best allocation of resources. Nevertheless, in so far as there is any desire for rational allocation of resources, every effort must be made to take into account all theoretically relevant factors determining the optimum distribution of resources.

After this digression on the allocation of resources to planning, let us return to "planning" itself and develop some concepts and categories with the help of which planning can be subjected to further analysis.

#### DIMENSIONS OF PLANNING

There are at least seven dimensions in terms of which planning can and should be analyzed and discussed: (1) significance; (2) freedom; (3) intensity; (4) time-span; (5) subject-matter; (6) area; (7) cost. Let us discuss these dimensions one by one.

*Significance.* Planning is always directed at some problem to be solved, or value to be realized, through recommended action. Depending on the social importance of the objective at which a specific planning activity is directed, that planning activity is more or less significant. Here again we meet an issue of value judgment: different persons may have different evaluations concerning the importance of a certain planning objective. When deciding on the allocation of resources between various planning activities, their relative significance is a crucial factor for determining priorities.

*Freedom.* No planning unit has complete freedom, in the sense of being permitted to reach any conclusion it thinks best. A limit is imposed by the accepted values of every society, which *a priori* exclude certain lines of action from consideration. Another limit is often set by the organic law setting up some planning unit, which may define the classes of recommendations open to the planning unit. From our point of view, any such formal, authoritative limitation of the freedom enjoyed by planning, is a *policy determination*.<sup>13</sup> Freedom of planning is a crucial dimension of the planning process: It is determined by

<sup>13</sup> The relative character of this concept of policy determination must be emphasized. What may be a policy determination from the point of view of a lower level, may be, from the point of view of a higher level, plan-execution. Other functions of policy determination are to determine the objectives of planning and to allocate resources between competing activities.

the interaction between basic social values, the power structure of the society and its adaptive needs.

Concerning the interplay between planning and policy determination, one must keep in mind that on one hand the policy determination often includes very vague terms, such as "reasonable," "in the public interest," etc. which in fact leave much freedom to the planning and executing units. On the other hand, planning influences policy determination and policy determination itself may be the subject-matter of planning.

*Intensity.* Depending on the ratio between allocated resources and the scope<sup>14</sup> of the planning activity, planning can be more or less intense. The concept of intensity is very important for evaluating correctly the planning activities of so-called "planned societies." While these societies may devote tremendous resources to central planning, the scope of the planning activity is so large, that the planning intensity may in fact be lower in many subject-matters than in so-called unplanned societies, where the resources allocated to planning are concentrated on a much more limited scope.

*Time-span.* Planning must deal with a certain, though not necessarily exactly predetermined, time-span. The selection of the optimum time-span for each planning activity depends on various factors, including the natural cycle of the subject-matter of planning, the acute need for interference to change an unbearable situation, limitations on our ability to predict the future,<sup>15</sup> our evaluation of present as against future needs<sup>16</sup> and more.

*Subject-matter.* Planning always deals with a delimited subject-matter, which is defined in terms of qualities, functions, social groupings or some other characteristics. Total planning, i.e., planning including within its subject-matter all extra-personal, inter-personal (and perhaps even intra-personal) activities, is unimaginable outside of fantastic science-fiction; the limitations of resources, the many competing alternative

<sup>14</sup> "Scope" includes time-span, subject-matter and area.

<sup>15</sup> This, of course, depends on the rate of social change and technological invention. On the other hand, the rate of change and invention depend to some degree at least, on planning.

<sup>16</sup> Edmund Burke in "reflections on the French Revolution" regards society as a "partnership between those who are living, those who are dead and those who are to be born." Such a social philosophy has important implications for the time-span to be considered in planning.

uses for them and the existence of strong opposition to planning of certain subject-matters—all these limit intensive planning at any given time to a selected, relatively small, number of subject-matters.

*Area.* The relation between planning and area is a rather complex one, which has at least three distinct, though closely interrelated, possible aspects. Since all human activity takes place in space-time, by its very nature planning must, and does, take into account this fact, and delimits its scope within these dimensions. Even in the few cases where the subject-matter of planning is not defined in territorial terms (e.g., "all slave trade"), the fact that all material phenomena are distributed in space, will make it convenient, and even inevitable, to use some territorial sub-division as units for delegated planning purposes.

To this general consideration on the inherent role of space in human thought and activity, a second aspect of the relation between area and planning must be added; the specific importance of territorial units in social affairs. Beginning with the nearly instinctive, emotional attachment of an individual to his place of birth, and going through all levels of social institutions, the special role of territory in social life is always apparent. It is true that today the individual's emotional attachment to specific pieces of land is weakened,<sup>17</sup> but this is more than compensated for in the predominant importance of territorial units as *units of organized social action*. The main unit of organized social action in contemporary society is the nation-state, which has an essential territorial basis. If we add to this the symbolic importance of territorial units<sup>18</sup>—"our" country, "our" state, "our" city and so on—the role of territorial units in social action seems to be basic and undeniable. As planning on the institutional level is mainly concerned with organized social action, and is itself often a form of such social action, there should be no doubt about the close relation between planning and territory.<sup>19</sup>

<sup>17</sup> This is a rather unique—and perhaps passing—feature of modern society which has very important implications for social planning.

<sup>18</sup> This symbolic identification must be kept distinct from the direct emotional attachment of a person to his birth-place, farm and so on.

<sup>19</sup> International planning does not constitute an exception. In so far as it is practiced, it reflects a transition in the basic territorial unit of action from the nation-state to the world-community. In fact, while international bodies do act



A third aspect of the relation between area and planning has its roots in the fact that one of the most important functions of every society is adjustment to its territory. Such adjustment is brought about to some extent by changing the physical environment and making the territory fit the needs of the society. In the field of planning this aim is reflected in the many planning activities having as their subject-matter certain aspects of what we call territory. Such "earth-bound" fields include resources conservation, flood control and many more.

In all these cases, the relation between area and planning poses two problems, the solutions of which have to be reconciled somehow. First, the *technical-optimum* area for dealing with the subject-matter of the planning activity must be defined; and second, this technical optimum area must be reconciled with the existing territorial units of social action and the limited freedom of the planning unit.

The best possible compromise between the two sets of areas will yield the *social-optimal* area for the designed planning activity.<sup>20</sup>

*Costs.* We have discussed the significance of planning, its intensity, its freedom and its scope in terms of time, subject-matter and area. One further dimension, *sui generis*, is costs. Costs enter planning in various ways and cross-cut some of the other dimensions. The allocation of resources to a certain planning activity is done in terms of permitted costs; the freedom of the planning unit may be limited in terms of permissible costs of plan-execution, and so on. Costs are also important from additional points of view. Manipulation of sums and costs is one of the chief forms of planning itself, and budgeting and accounting is a most important form of communication between policy determination, planning and plan-execution.

Having discussed the concept of planning and some of its

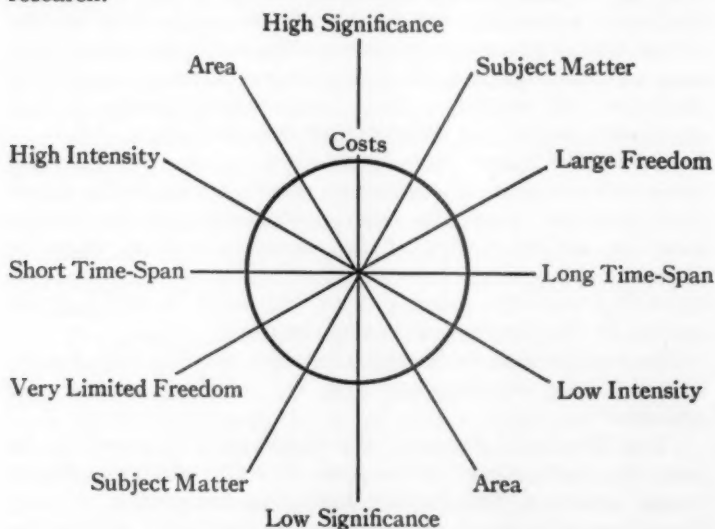
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as planning agencies, the plan-execution and much delegated planning is as yet nearly always in the hands of the nation-states.

<sup>20</sup> It is incorrect to regard the technical-optimal area as the "desirable" area of action which is "distorted" by the "unfortunate" existence of nations, states, local units, etc. We have already mentioned the psychological importance for human happiness of emotional attachment to territories and the inevitability of territorial units of social action and their role in planning. Here it should be emphasized that these existing territorial units of social action have to play the most significant role in planning: The most important initiators are those who can mobilize loyalty, resources and support. The planner cannot and must not neglect these human and moral facts in favor of the "social engineering" approach.



dimensions (which are summed up in the diagram below), we are still faced by the necessity to distinguish between planning and some related processes, including plan-execution and research.



#### PLANNING AND RELATED PROCESSES

There are three closely interrelated and constantly interacting social processes which must be kept analytically distinct: awareness of the need to plan, which is an essential prerequisite of planning, planning itself and plan-execution, through which planning exerts direct influence on social events.<sup>21</sup>

Awareness of the need to plan presupposes a belief in the effectiveness of planning, based partly on earlier direct and indirect experience with planning on the individual and institutional level,<sup>22</sup> and on an awareness of the existence of a problem which might be dealt with through planning. On the other

<sup>21</sup> We shall deal here with planning on the institutional level. Examination of the interaction of various activities on the individual level would lead us too far into the field of neurology and psychology.

<sup>22</sup> An interesting problem is to what extent institutional planning has its roots in individual experience with planning of private affairs, which is transferred by the individuals to the institutional level.

hand, planning itself may show the existence of unsuspected factors and additional problems which have to be dealt with. In this sense, planning can be regarded as self-perpetuating: it always finds further subject-matters and problems that need even more planning.<sup>23</sup>

The relation between planning and plan-execution is manifold and includes many complex elements: The conclusions reached through planning must be communicated to the persons and institutions in charge of plan-execution.<sup>24</sup> This poses very difficult problems of communication; in most cases the planning conclusions are rather complex and include many "ifs" and "whens," very difficult to express and convey through written symbols. Even in the few cases where the planning conclusion can be put in the form of detailed directions for action, much discretion must be left to the various executing bodies who have to adapt general standards and rules to particular and unpredictable circumstances. Unless the plan executors are very familiar with the unwritten spirit of the plan, plan-execution will often diverge from the intentions of the planners. Many devices are used to overcome this difficulty; one of them is to put one organization in charge both of planning and some phases, at least, of plan execution. Another, often used, solution is to give the planning unit a significant device of direct authority over the plan-executing units, so as to insure quick correction of any straying from the right path.<sup>25</sup>

Planning itself is constantly influenced by plan-execution. The plan-executing bodies are one of the most important sources of information for the planning body on the facts of the situation, occurring changes, appearance of unexpected results and other facts which need to be taken into account in replanning and further planning.

<sup>23</sup> This, taken together with the general self-perpetuating inertia and empire-building tendencies of bureaucratic structures, makes it very necessary indeed to re-examine periodically all planning activities in order to check whether the principle of optimal use of limited resources is complied with.

<sup>24</sup> Planning conclusions can be put in the form of "Master Plans," "X Years Plans," budgets, concrete work assignments, etc. Often the freedom of the planning body is restricted not only to certain substantive recommendations, but also to specific forms of presenting the conclusions and communicating them to the decision-making and the plan-executing units.

<sup>25</sup> In fact, nearly every administrative unit engages both in planning and in plan-execution; the difference is one of degrees. Similarly, the distinction between planning and plan-execution is an analytical one; there are marginal activities which can be regarded as belonging to either of these categories.

The continuous character of both the planning process and plan-execution, and the distribution of planning and plan-executing functions between various units on different levels of action, complicate the picture beyond description. The problems of communication involved seem nearly unsolvable and the surprising thing seems to be that planning works at all.<sup>26</sup> Where successful planning does take place, this may be due to a large extent to the helping hand of various informal factors, the "informal organization," which supplements the inadequacies of formal channels of communication.<sup>27</sup>

"Plan execution" can take various forms: It can take the form of no-action, when the planning-conclusion is that the best way to deal with a certain matter is to leave it alone; this may be so, either because the net effect of any interference would be undesirable, or because the dangers of unexpected undesirable results are too great,<sup>28</sup> or because the expected desired results are not worth the resources necessary for plan-execution.<sup>29</sup>

Very often, plan-execution involves planning on a lower level. In this case, what is a planning activity, from one point of view, constitutes at the same time (viewed from another level) part of a scheme for plan-execution. In fact, in all but the simplest situations, planning with regard to a certain subject-matter is distributed between various units on different levels.

Here it is necessary to introduce another important distinction, namely that between *autonomous* and *delegated planning*. Delegated planning is planning which constitutes plan-execution from the point of view of another planning unit; autonomous planning is planning pursued not as part of any higher-level plan.<sup>30</sup>

<sup>26</sup> It may be that much of what goes under the name of "planning" is in fact not much more than predictions of what is going to happen in any case. An impressive "Five Year Plan" may in fact be anything but a coordinated, over-all, rational plan; rather it may be a collection of different uncorrelated plans and prediction. Cf. Michael Polanyi: *The Logic of Liberty* (1951), p. 133 *et seq.*

<sup>27</sup> There is much need and scope for intensive research on this aspect of communication and formal organization.

<sup>28</sup> In this sense, it is certainly true that bad planning is worse than no planning.

<sup>29</sup> It seems that very seldom has planning come to the conclusion that no-action is the best way. This may be due to the fact that resources are allocated to planning only when it is clear that some action is called for. Furthermore, it may be that planning units in general have a tendency to try to justify their work by reaching conclusions showing the need for positive action.

<sup>30</sup> The importance of this distinction can be illustrated by applying it to a con-

At this stage, we may return to the point made earlier, that it is much easier to get agreement on planning than on plan-execution. Planning is a rather neutral function,<sup>31</sup> but plan-execution involves concrete interference sure to be opposed by many interests. There is a lot of difference between agreeing to have a problem thought over, and agreeing to concrete conclusions reached by someone else's thinking. For this reason it is necessary to have the decision-making bodies approve the planning-conclusion, even after they have agreed to submit a matter to planning.<sup>32</sup>

In addition to awareness of the need to plan and plan-execution, there is at least one process which is so closely related to planning, that it must be mentioned here: research. Research includes systematic thought and action oriented towards enlarging our knowledge. It is essential for planning and often closely associated with it, but should not be identified with it.<sup>33</sup> Research enlarges our knowledge of social processes in general. Basic research provides the necessary basic systematic knowledge on which all rational planning is based. Successful planning depends also on knowing all the relevant facts about the subject-matter. Specific research projects may be initiated and executed, sometimes by the planning unit itself, in order to get the necessary raw material for the planning activity. Furthermore, investigation of the results of plan-execution is necessary for corrective planning.

On the other hand, planning itself is an important subject-matter for research. Investigation of the planning process, plan-execution etc., provides the knowledge and understanding

crete issue, namely the optimum scope of city planning. Some authors (e.g., Walker, *op. cit.*) rely on the precedent of large-scope city planning during the depression to justify large-scope city-planning today. But it seems that much of the enlarged scope of city planning at that period was *delegated* planning, part of a national plan to relieve unemployment and rehabilitate the economy. Therefore what happened then is largely irrelevant to the problem, whether in the absence of national planning in some matters, cities should deal with them through *autonomous* planning.

<sup>31</sup> In many cases some of the conclusions of planning are predicted; in these cases groups who oppose certain expected or possible planning conclusions try to interfere at an earlier stage and oppose planning itself.

<sup>32</sup> Various efforts by enthusiastic planners are devoted to inventing devices designed to prevent decision-making bodies from interfering with plan-execution once a matter has been submitted to planning. For an extreme attack on the unsuitability of legislative bodies to reconsider planning conclusions see Rexford G. Tugwell: *The Place of Planning in Society* (1954).

<sup>33</sup> Cf. John D. Millett: *Management in the Public Service* (1954), p. 73 *et seq.*

necessary in order to improve the planning function itself. It is also time, that research itself be planned to deal with matters which are significant, to prevent overlapping, insure free and full communication, etc.

#### THE PLANNING UNITS

We have mentioned two categories of planning-units: Individuals and institutions. We must now distinguish between various kinds and forms of institutional planning units.

It should be clear by now that planning, as defined in this paper, takes place within all social units: the Club Committee, the Church Social Affairs Council, the Scout Fireside Meeting, all when discussing their programs of action engage in planning, though generally on matters of low significance for the community as a whole. Much significant planning of high intensity goes on in business, especially in the big corporations, but most of the significant institutional planning in contemporary society is done by the various units of government.<sup>34</sup> One extra-governmental institution which serves as an important center for very significant long-term planning are the Universities; today at most Universities individuals and groups engage both in research and action-oriented thought on very important social problems.<sup>35</sup> The importance of these planning units is augmented by the freedom enjoyed by their personnel and their high caliber; it is of central social importance to preserve the independence and freedom of the Universities as centers of such long-term planning.

Concerning planning in Government, the problem is one of the optimum allocation of planning functions between various divisions and levels of government. It is especially important to bear in mind, that all the divisions of government, including the judiciary, share in the planning function.<sup>36</sup> In general, attention has been devoted mainly to the planning function of the executive, while the special problems of planning by the legislature and the judiciary, and the need to provide better

<sup>34</sup> The relative significance of planning on the individual and the institutional level varies from subject-matter to subject-matter and between different regimes.

<sup>35</sup> The book by Charles McKinley, *Uncle Sam in the Pacific Northwest* (1952), can serve as an illustration of important planning work done by individuals associated with Universities.

<sup>36</sup> Cf. Arthur Taylor Von Mehren: "The Judicial Process in the United States and Germany." *Festschrift für Ernst Rabel*, Volume I, p. 67 et seq. (1954).

facilities for planning by these bodies, has been rather neglected.<sup>37</sup>

Much thought has been devoted in the United States to the allocation of autonomous and delegated planning functions between various levels of government.<sup>38</sup> Here, the problem is one of determining the optimum level for planning of various aspects of social life, which is closely related to the larger problem of the optimum area for social action in a certain matter.

This paper does not propose any solution to the substantive and organizational problems of planning; neither does it deal directly with larger issues of social philosophy dealing with the relation between planning, freedom and various other basic values. Rather than engage in polemics on these controversial issues, it was our intention to provide a conceptual and analytical scheme which, it is hoped, may help to overcome semantical difficulties and emotional blocks, and thus make it easier to examine the really significant issues of planning faced by all contemporary societies.

<sup>37</sup> Some important remarks and bibliographic annotations on this matter can be found in John M. Gaus: "The Planning Process in Government," published in T. C. T. McCormick (ed.): *Problems of the Postwar World* (1945), p. 163 *et seq.*

<sup>38</sup> This is not equally true for all divisions of Government; e.g., it is doubtful whether the allocation of functions (including their planning element) between the levels of the federal and state judiciaries has been sufficiently considered.

## THE LEGISLATIVE VETO: ITS PROMISE AND ITS PERILS

*Joseph Cooper*

FOR the purposes of this paper the legislative veto will be defined as a statutory provision rendering the effectuation or the continued effectuation of actions proposed by the executive in pursuance of the statute subject to some further form of legislative assent. Thus the implementation of a statute is made contingent on some further positive or negative expression of legislative approval. Such approval or non-approval has to be expressed within a specified period, exists as the condition of any administrative functioning and remains free of Presidential veto.<sup>1</sup>

So defined the actual form the veto takes in a statute can vary greatly depending on the way in which four different sets of variables are combined. The veto may be exercised in a "before the fact" or "after the fact" manner. That is, the executive action may go into effect immediately though kept subject to subsequent disallowance for a limited period; or the

<sup>1</sup> As defined in this paper the legislative veto mechanism does not include the following arrangements:

- 1) Termination or repeal of statute by a form of legislative action not subject to presidential veto, e.g., the Defense Production Act of 1950 (64 Stat. 822), the Federal Civil Defense Act of 1950 (64 Stat. 1249), the Lend Lease Act of 1941 (P.L. 11, 77th Cong., 1st Sess.), and the Economic Cooperation Act of 1948 (62 Stat. 155).
- 2) Termination of administrative action by a form of legislative action not subject to presidential veto, e.g., the Greek-Turkish Aid Act of 1947 (61 Stat. 105), the Mutual Defense Assistance Act of 1949 (63 Stat. 80), and the Universal Military Training and Service Act of 1951 (65 Stat. 80).
- 3) Compelling or initiating executive action by a form of legislative action not subject to presidential veto, e.g., the Neutrality Act of 1939 (54 Stat. 4), and the Federal Highway Act of 1944 (58 Stat. 839).
- 4) Removal of executive officers by a form of legislative action not subject to presidential veto, e.g., the T.V.A. Act of 1933 (48 Stat. 60) and the Budget and Accounting Bill of 1920 (H.R. 9783, 66th Cong., 2nd Sess.)—see veto message, 59 Cong. Rec. 8609.
- 5) Legislative veto action over proposals originating outside the Executive Branch, e.g., the Federal Civil Defense Act of 1950 (64 Stat. 1249), the Administrative Rules Bill of 1951 (S. 17, 82nd Cong., 1st Sess.), the District of Columbia Home Rule Bill of 1948 (H.R. 4902, 80th Cong., 2nd Sess.), the Federal Rules of Civil Procedure Act of 1934 (28 U.S.C. § 2072), and the Federal Rules of Criminal Procedure Act of 1940 (18 U.S.C. § 3771).

*A priori*, all of the above could be called instances of the legislative veto mechanism. However, this paper has excluded these arrangements from the definition in order to concentrate on that one arrangement which bears the most significance as a developing weapon for insuring administrative accountability.



executive action may not go into effect until it has been subject to disallowance for a limited period. Moreover the person or body that wields the device may vary. It can be vested in either the whole Congress, one House of the Congress, the committees of the Congress or even the committee chairmen. In addition the veto may be negative, affirmative or deliberative in nature. In the first instance action proposed by the executive goes into effect or remains in effect unless negated within a specified time. In the second instance action proposed by the executive goes into effect or remains in effect if it is affirmed within a specified time. In the third instance action proposed by the executive does not go into effect unless it has lain before Congress for a specified time. Here, theoretically, the veto has to take the form of regular legislation; but in reality many of the committees of Congress are so strong that the mere hint of their disapproval is enough to stop action. Lastly, either a simple or a constitutional majority may be required to put the veto into effect.

The veto, as we know it today, remained uncrystallized in form until 1939. The Reorganization Act of that year climaxed two decades of trial and error with respect to the device and for the first time systematically combined all the integral features of the veto in one mechanism.<sup>2</sup> This measure authorized the President, acting as an agent of the Congress, to re-group agencies and functions within the Executive Branch subject to Congressional disapproval by concurrent resolution within sixty days. In addition, care was taken to ward off minority control by including cloture and non-amendability in the act. Since that time some twenty other acts have contained veto provisions.<sup>3</sup> Included in this group are such significant

<sup>2</sup> P.L. 19, 76th Cong., 1st Sess.

<sup>3</sup> They are as follows: The Reorganization Acts of 1945, and 1949, the Alien Registration Act of 1940, the Surplus Property Act of 1944, the Atomic Energy Acts of 1946 and 1954, the Federal Airport Act of 1946, the Displaced Persons Act of 1948, the Defense Land Transfer Act of 1951, the Military and Naval Construction Act of 1952, the Rubber Producing Facilities Disposal Act of 1953, the Refugee Relief Act of 1953, the Lease-Purchase Act of 1954, the Small Watershed Act of 1954, the Interior Department Appropriation Act of 1954, and the Defense Appropriation Act of 1956. In addition, in 1944 naval land transfers and certain types of naval petroleum development contracts were subjected to committee approval. In 1948 an act was passed which required repayment contracts negotiated by the Secretary of Interior for rehabilitation and betterment work on irrigation systems to lie before the House and Senate Committees on Interior and Insular Affairs for sixty days before taking effect. In 1952 & 1953 acts were

measures as the Reorganization Acts of 1945 and 1949,<sup>4</sup> the Rubber Producing Facilities Disposal Act of 1953,<sup>5</sup> the Atomic Energy Acts of 1946 and 1954,<sup>6</sup> and the Small Watershed Act of 1954.<sup>7</sup> Concomitantly, unsuccessful attempts have been made to apply the veto to such varied fields of legislative endeavor as F.E.P.C., reciprocal trade, valley authorities, price control, public housing, postal rates, public building construction programs, and Commodity Credit Corporation operations.<sup>8</sup>

On the whole the device has been used most extensively as a weapon for checking administrative management and operations. Indeed, in the last six years 70 per cent of all veto utilizations have been wholly or significantly concerned with performance.<sup>9</sup> The explanation lies in the fact that Congress has fallen back on the veto as a means of preserving its control in those areas where the exercise of granted negotiating authority by executive agencies involves the Federal Government in obligations which cannot subsequently be effectively checked through the appropriations process. As the House Appropriations Committee put it last year speaking in favor of a measure which would have subjected Housing and Home Finance Agency project contracts to veto review, "The Committee is greatly concerned over the lack of Congressional control over some of the loan and grant programs. During the past few years Congress has lost control over the expenditure of

passed which subjected rent adjustment in Federal housing provided for Governmental employees to approval by the Chairman of the House Appropriations Committee. This list of measures does not include renewals of previous pieces of veto legislation nor amendments thereof contained in other pieces of legislation which do not add substantively to the degree of veto control.

<sup>4</sup> P.L. 263, 79th Cong., 1st Sess.; P.L. 109, 81st Cong., 1st Sess.

<sup>5</sup> P.L. 205, 83rd Congress, 1st Sess.

<sup>6</sup> 60 Stat. 764 (1946); 68 Stat. 919 (1954).

<sup>7</sup> P.L. 56, 83rd Cong., 2nd Sess.

<sup>8</sup> Of minor importance are three other failures at control through the veto. In 1946 an attempt was made to subject the Navy's choice of vessels for the Bikini tests to committee approval. In 1953 a bill was introduced which subjected any transfer of T.V.A. headquarters from Knoxville, Tennessee to disapproval by concurrent resolution. A provision for committee approval was also contained in the Camp Blanding Land Conveyance Act of 1954 which was vetoed by the President for that very reason.

<sup>9</sup> Since 1939 the veto has been directed to performance with regard to surplus property disposals, rubber plant disposals, military real estate transactions, military construction projects, lease-purchase contracts, small watershed projects, certain naval petroleum contracts, airport construction projects, rent adjustment in Federal housing for Government employees, and concession and repayment contracts negotiated by the Secretary of the Interior.

approximately \$3.3 billion by granting Treasury authorizations and the right to make binding contracts before money is appropriated."<sup>10</sup> Though the attempt at veto review failed in this case, in seven other instances over the last seventeen years the veto has been used to surmount the oversight barrier created by breach of contract.<sup>11</sup> Two recent illustrations are the Defense Land Transfer Act of 1951 and the Rubber Producing Facilities Disposal Act of 1953. The latter permits either House of Congress to strike down proposed disposals of Government-owned synthetic rubber plants for a period of 60 days after the disposal contract has been submitted to the Congress.<sup>12</sup> The former requires the military departments to secure committee approval for land purchases of \$25,000 or more, leases with annual rents of \$25,000 or more, or real estate transfers of property with a value of \$25,000 or more.<sup>13</sup>

The veto has also been used in measures which emphasized the policy aspects of administrative decision-making.<sup>14</sup> But nearly one out of every two utilizations of the veto for purposes of policy control has either involved Governmental reorganization or has had significant performance as well as policy implications. Both the Rubber Producing Facilities Disposal Act of 1953 and the Surplus Property Act of 1944 were as much concerned with insuring the Government a fair return as with preventing monopoly in the industries involved.<sup>15</sup>

With regard to structure, though no piece of veto legislation

<sup>10</sup> H. Rept. No. 304, 84th Cong., 1st Sess., pp. 9-10.

<sup>11</sup> The seven include veto review of naval petroleum contracts, surplus property disposals, Interior Department irrigation repayment contracts, rubber plant disposals, concession contracts for the National Parks, military real estate transactions, and lease-purchase contracts.

<sup>12</sup> The Rubber Producing Facilities Disposal Act is not directly related to the point made in the Appropriations Committee report since it is concerned with disposals, not expenditures. Nonetheless, it belongs in the same category as the Defense Land Transfer Act and the unsuccessful H.H.F.A. veto. For granted negotiating authority can involve the receipt as well as the expenditure of funds, and in either case once Congress grants negotiating authority, the legal problems raised by breach of contract inhibit subsequent Congressional control over the actual provisions of contracts concluded in fulfillment of such authorizations.

<sup>13</sup> 65 Stat. 365 (1951).

<sup>14</sup> Since 1939 the veto has been directed to policy in the following instances: the Alien Registration Act of 1940, the Reorganization Acts of 1939, 1945, and 1949, the Surplus Property Act of 1944, the Atomic Energy Acts of 1946 and 1954, the Displaced Persons Act of 1948, the Refugee Relief Act of 1953, the Defense Appropriation Act of 1956, and the Rubber Producing Facilities Disposal Act of 1953.

<sup>15</sup> 58 Stat. 775 (1944), 59 Stat. 546 (1945).

has ever provided for "after the fact" control, all the other possible variations in form have found expression in law. Congressional approval has taken affirmative, negative, as well as deliberative forms on numerous occasions. Note the Military and Naval Construction Act of 1952<sup>16</sup> (committee affirmation), the Refugee Relief Act of 1953<sup>17</sup> (two-House affirmation), the Defense Appropriation Act of 1956 (committee negation), the Reorganization Act of 1945 (two-House negation), the Reorganization Act of 1949 (one-House negation), the Surplus Property Act of 1944 (waiting-period) and the Interior Department Appropriation Act of 1953<sup>18</sup> (waiting-period review for concession contracts). Nor, as is evident from the above, have the one or two House forms suffered from neglect though, as might be expected considering the fact that the majority of veto utilizations have been directed toward performance, in most instances the committees have been the wielders of the veto. Note the Lease-Purchase Act of 1954,<sup>19</sup> the Small Watershed Act of 1954, the Defense Land Transfer Act of 1951, *et al.* In the case of rent adjustment in Government housing provided for Federal employees the veto has even been vested in a committee chairman.<sup>20</sup> Similarly, in 1950 an act requiring committee approval for Interior Department irrigation repayment contracts was amended to permit approval of these contracts by the Chairmen and ranking members of the House and Senate Committees on Interior and Insular Affairs whenever Congress is not in session.<sup>21</sup> Lastly, upon occasion the constitutional majority form has been included as part of the veto mechanism. For example, the Reorganization Act of 1949 requires an absolute rather than a simple majority to put disapproval resolutions into effect.

#### PROBLEMS OF CONSTITUTIONALITY

Throughout its history the charge of unconstitutionality has been raised against the veto. The constitutional case against

<sup>16</sup> P.L. 534, 82nd Cong., 2nd Sess. See also 58 Stat. 190 (1944).

<sup>17</sup> P.L. 203, 83rd Cong., 1st Sess.

<sup>18</sup> P.L. 172, 83rd Cong., 1st Sess.

<sup>19</sup> P.L. 519, 83rd Cong., 2nd Sess.

<sup>20</sup> P.L. 547, 82nd Cong., 2nd Sess.; P.L. 207, 83rd Cong., 1st Sess.

<sup>21</sup> 62 Stat. 724 (1948); 64 Stat. 11 (1950).

the veto rests on three props.<sup>22</sup> First, it is argued that Congress cannot take "legislative" action without Presidential approval. This argument, however, is dated; and even the Attorney General's Office, by necessity a frequent leader in the fight to strike down the veto on constitutional grounds, has admitted as much. A memorandum issued by that office in 1949 affirms the view that "legislative" action not subject to Presidential approval is still constitutional if provided for in the enabling act. In short, such "legislative" action is permissible if it exists as a condition in the original statute.<sup>23</sup>

Second, it is contended that the veto mechanism permits law making powers of the whole Congress to be exercised by one of its parts. This argument is very convincing when applied to the committee action form, but its range is much more extensive than this. Thus, some would contend that the two-House veto allows one-House to act for the whole Congress since an executive proposal goes into effect unless negated by both Houses. Conversely, others maintain that the one-House veto errs since it enables a single House to strike down an executive proposal. And a few even argue that only the two-House affirmative form truly satisfies the requirement of action by the whole Congress. However, none of these latter contentions seem valid to this writer. When the veto is properly used and structured non-negation can rightly be seen as an indication of implicit approval. Moreover, both the one and two House vetoes represent action by the whole Congress. Congress in each instance is entitled to decide how its disapproval is to be expressed. In those instances where vigorous control is desired it may justifiably stipulate non-negation by both Houses. That is, that action cannot go into effect if either House disapproves. In those instances where less vigorous control is desired it may justifiably stipulate non-approval by both Houses. That is, that action goes into effect unless disapproved by both Houses.

Third, and this is really the crux of the constitutional case against the veto, it is argued that the veto vests legislative functions in the executive and/or executive functions in the

<sup>22</sup> Perhaps the best statement of the constitutional case against the veto can be found in Robert W. Ginnane's, "The Control of Federal Administration by Congressional Resolution and Committees," *Harvard Law Review*, February, 1953.

<sup>23</sup> S. Rept. No. 232, 81st Cong., 1st Sess., pp. 19-20.

legislature.<sup>24</sup> This argument can be stated in either an *a priori* or an *a posteriori* fashion.

*Forms of the Argument.* In the *a priori* form an attempt is made to draw a clear and conclusive distinction between executive and legislative functions. As stated by the Supreme Court in *Wayman v. Southard*, the proposition is that "the Legislature makes, the Executive executes, and the Judiciary construes the law."<sup>25</sup> As reiterated in *Springer v. Philippine Islands* (1928), the argument rests on the notion that "the powers conferred on each of the three departments are exclusive in character."<sup>26</sup> On this basis it is contended that an act such as the Reorganization Act of 1939 vests legislative functions in the executive and/or that a provision such as Section 638 of the Defense Appropriation Act of 1956 vests executive functions in the legislature.<sup>27</sup> This section subjects disposals of production and commercial facilities owned and operated by the Department of Defense to committee approval.<sup>28</sup>

The defect in this approach lies in its inability to see the large amount of imprecision necessarily inherent in the notions of legislative and executive functions. Policy and performance form a continuum with one predominating at one end and one at the other. Policy shades into performance as general decisions are translated into specific acts through progressive application; but they never exist completely apart except at the absolute ends of the continuum. Instead, they exist as merely

<sup>24</sup> This is the only part of the constitutional case against the veto that could conceivably apply to the waiting-period form as well.

<sup>25</sup> 10 Wheaton 1 (1825).

<sup>26</sup> 277 U. S. 189 (1928).

<sup>27</sup> The most recent statement of this position was made by Attorney General Brownell with regard to Section 638 of the Defense Appropriation Act of 1956. See 60 *Dickinson L. Rev.* 1 (1955). All together as of June 2, 1956, the Government owned 19,771 business enterprises employing 258,425 civilians and having capital assets of over \$11 billion. The capital assets of enterprises owned and operated by the Government are slightly less than \$3 billion with the Department of Defense accounting for all except \$700,000.

<sup>28</sup> P.L. 157, 84th Cong., 1st Sess. Section 638 states that "No part of the funds appropriated in this act may be used for the disposal or transfer by contract or otherwise of work that has been, for a period of three years or more performed by civilian personnel of the Department of Defense unless justified to the Appropriations Committees of the Senate and House of Representatives, at least ninety days in advance of such disposal or transfer, that its discontinuance is economically sound and the work is capable of performance by a contractor without danger to the national security: *Provided*, That no such disposal or transfer shall be made if disapproved by either committee within the ninety-day period by written notice to the Secretary of Defense."



two aspects of the same whole. For this reason the categories of enactment and execution can never be absolute. They must be somewhat arbitrary. As Paul Appelby has remarked, what to do and how to do it are always one problem though the problem is of a different order at different levels of abstraction.<sup>29</sup> If we label one aspect of the problem "enactment" and the remainder "execution," the intermingling of policy and performance is not destroyed. Rather, the problem has simply been divided up and parcelled out with one part of the intermingled whole going to the executive and the other to the legislature.

Of course, a broad distinction can be drawn between legislative and executive functions. Democracy demands both that the most basic and most vital decisions be made by the legislature and that the bulk of the operational aspect of government be done by the executive. It is even true that on the basis of the above distinction one is warranted in reserving the term "law" to the policy decisions of the legislature. Nevertheless, the distinction between legislative and executive functions, though valid in a relative and theoretical sense, cannot provide a criterion for delimitation which is widely applicable. For since the distinction is in essence one of degree resting on the importance of the decisions involved, functions "properly legislative" or "properly executive" in nature cannot be identified with surety in the vast majority of cases. How does one distinguish between the decisions the President made under the Reorganization Act of 1939 and those he made under the Federal Reporting Act of 1942?<sup>30</sup> How does one distinguish between appropriation riders which forbid Veterans' Hospitals to use butter substitutes except for cooking purposes and appropriation riders which forbid certain disposals unless approved by Congress?<sup>31</sup> How does one distinguish between Congressional operations with regard to printing, accounting, the Capitol grounds, etc., and Congressional surveillance of concession contracts negotiated by the Secretary of the Interior for the National Parks? How does one distinguish between the regulations of the I.C.C. and the price-fixing powers of the

<sup>29</sup> Paul Appelby, *Policy and Administration* (University, University of Alabama Press, 1949), Chap. I.

<sup>30</sup> 56 Stat. 1078 (1942).

<sup>31</sup> 53 Stat. 545 (1939).



Secretary of Agriculture? In each of these cases is it demonstrable that the former action is "properly legislative" and the latter "properly executive?" Yet if not, there is no basis for the claim that functions are exclusive, definite, or certain in terms of their inherent nature.

In other words, in the preponderant number of instances Congress has to rely on practical guides to distinguish those areas of policy and performance that are properly reserved to the legislature. And this is as it should be since the level of abstraction at which a problem is divided must be a function of its political significance. This is not to say that one cannot question the wisdom of the legislature's particular divisions. To be sure, one can. It is only to say that one cannot question them in terms of absolute and precise categories since gradations can never be split into their pure components. In *Yakus v. U. S.* (1944) the Court perceived that a division of powers does not and cannot involve an exclusive division of functions and its decision, which permits action to be seen as executive in nature if a standard is contained in the original statute, stands as an explicit recognition of such a perception.<sup>32</sup>

The *a posteriori* form of the argument makes no *a priori* distinction between "properly legislative" and "properly executive" functions. Realizing that the Congress also negotiates contracts and that the executive also determines policy, it would leave the identification of legislative and executive functions to Congressional volition. What is contended is that Congress cannot check through the veto what it has already defined as an executive function in the statute.

This argument is potent but not overwhelming. One could argue that the power to set standards of administration covers the power to review, reject and forbid their practical application without repealing the act in which the standards were set.<sup>33</sup> In addition, in what way does the process of holding the executive accountable through the veto vest executive functions in the Congress? In terms of scope or effect the veto does essentially what other instruments of Congressional control do. Appropriations, for example, can be and are used to supervise details, to prevent the implementation of execu-

<sup>32</sup> 32 U. S. 414 (1944).

<sup>33</sup> Arthur Krock, "In the Nation," *New York Times*, July 15, 1955.

tive actions, and even to paralyze executive discretion. Yet no one has ever argued that the appropriations process vested executive functions in the Congress. Now are the differences between the veto and a device like appropriations of such a nature as to validate the claim that the veto vests executive functions in the Congress? The answer is decidedly not. Though the appropriations process requires explicit approval, non-negation can be construed as approval if the veto is properly framed. Though the veto reverses the legislative process, such a reversal exists as a condition of the original legislation.

*The Veto and the Constitution.* In conclusion, the Constitution will not destroy the veto mechanism. Even if all the above arguments fail to render the veto invulnerable to assault on constitutional grounds, the device, as a last resort, can crawl behind the appropriations process. In so doing the veto becomes virtually untouchable since appropriations control constitutes the ultimate and basic safeguard of representative democracy. With regard to federal grants-in-aid for airport construction, lease-purchase of public buildings, and small watershed projects, the very authorization acts forbid any appropriation for executive actions in pursuance of the statutes until such actions have been subject to veto review. In other instances where it is not possible to tie the veto to the appropriations process through the language of the authorizing act, the veto can still be grafted on the appropriations process through the use of riders as was done in the case of concession contracts for the National Parks and disposals of Defense Department production facilities.<sup>34</sup>

However, in all probability such a drastic retreat will not be necessary. Only the committee-action form is greatly vulnerable to attack on constitutional grounds and even here there is not much chance that the attack will ever be mounted since the cost of success would make any victory a Pyrrhic one. As George Mahon (D., Tex.), Chairman of the House Subcommittee on Defense Appropriations, recently put it, "No, no,

<sup>34</sup> Under this rider only six disposals out of about fifty have been vetoed by the House Appropriations Committee. Among the facilities saved were ropewalk and chain manufacturing at the Boston Naval Shipyard and paint manufacturing at the Norfolk and Mare Island Shipyards. However, on May 10, 1956 the House by a vote of 222 to 156 knocked this rider out of the Defense Appropriation Act of 1957. At the time of this writing the matter is still pending before the Senate.

I do not expect the President and the Department of Defense to put our vetoes to a court test. The President made a rather rash statement last July 13, but officials in the department well know that they cannot afford to do other than cooperate reasonably well with the Appropriations Committees of Congress. The Appropriations Committees have tremendous power, as you well know, and officials of the Department of Defense, as a general rule, have a disposition to cooperate in a very fine way and in a very fine spirit."<sup>35</sup> In truth, constitutional arguments most often play an instrumental role rather than expressing heartfelt convictions about the eternal verities. Thus, Presidential cries of unconstitutionality have always been directed against the committee-action form and never against the one- or two-House forms even though logically checking a rubber plant disposal through a one-House veto is as much a usurpation of executive functions as checking Defense Department production plant disposals through a committee veto. Thus, Carl Vinson (D., Ga.), Chairman of the House Armed Services Committee, has been a most adamant defender of the constitutionality of his committee's veto over military land transfers though he has vigorously objected to the Appropriations Committee veto contained in Section 638 of the Defense Appropriation Act of 1956 on the grounds that it "trespassed on executive functions."<sup>36</sup>

#### PRACTICALITY AND PRINCIPLE

As with so much else in American government only the demands of practicality adequately explain the past course of Congressional veto utilization and the sequence of executive criticism of such utilizations. Congress, faced with a bureaucracy expanded in size and scope, has groped spasmodically for this new means of control. The Presidency, on the other hand, fearful that the device would serve as a means for over-extending legislative oversight, has opposed the most noxious instances of its use and has pressured the Congress to circumscribe the form of its expression and the sphere of its operation. As a result the device has been developed and elaborated in terms of a continuing pragmatic interplay between the Congress and the Presidency.

<sup>35</sup> Letter to Joseph Cooper, March 23, 1956.

<sup>36</sup> 97 Cong. Rec. 5436; 101 Cong. Rec. 5308 (Unbound, May 12, 1955).

However, it has not been a practicality of the highest or the wisest kind. To understand why we must first examine the proper roles of the executive and the legislature in American government and the principles that should direct their relationship.

*Proper Roles of the Respective Branches.* In both enactment and execution the job of the executive branch is to lead. The process of formulating and enacting public policy reflective of community needs is a matter of reducing alternatives and concentrating on more promising possibilities. This the executive is better able to do than the legislature. It has access to vast stores of administrative information and expertise; it is learned in the problems of doing; and it can draw more sagaciously on past administrative experience. More important, the executive is better able to organize itself to provide central and coherent direction of the enactment process than is any form of legislative leadership. If a legislature wishes to provide its own leadership without making that leadership a part of the executive, a dispersal of function and power is necessary. For example, without an effective committee system legislative leadership would be impossible since there would be no adequate source of information and expertise available to the legislature. Yet to give power and function to these committees is to make subsequent integration more difficult. In short, patterns of legislative leadership are largely self-defeating. The very means of organization, expertise, and information become obstacles to coordination and function as such roughly in direct proportion to the extent to which they successfully function as units for increasing legislative competence. The tendency then under legislative leadership is always toward non-integration of policy and capitulation to the special interests.

But, no matter how inspired executive leadership may be, the legislature still has a vital and indispensable role to play in the enactment process. It makes both a functional and a qualitative contribution to the realization of the constitutional democratic ideal.

In enactment the legislature serves as an integrating agency through which the policy of the government and the claims of the various groups and interests are brought together and

meshed.<sup>37</sup> In so doing the legislature provides the executive with an essential criterion for its dual, though overlapping, task of translating the general programs of the President into specific legislative acts and reconciling interest group demands with the broader interests of the nation. For although the executive may utilize data and standards provided by the parties, interested pressure groups, and its own departments, nonetheless, the executive has no better index of the degree to which its proposals are actively or passively acceptable to the nation than the voice of the legislature. In other words, the executive needs the guidance that the legislature can provide because no other institution either public or private is as well-adapted to serve as the political barometer of the community. Composed of a large number of men drawn from all parts of the country, it is the most sensitive instrument of public opinion in the state. It can serve effectively as a focal point for the expression and organization of opinion, especially since the opposition party is always more than ready to function as a rallying point for discontent.

Nor is the legislature's adjustive or harmonizing contribution the sole justification for its policy role. Without a legislature there would be no guarantee that executive proposals would be adequately subject to modification by public opinion. The constraint provided by four-year elections is not intense enough to insure the amount of executive policy adjustment that popular control over enactment demands unless it is supplemented by legislative criticism and control. In the words of Elaine Tanner, the legislature institutionalizes the "open mind," the capacity for rational change in government.<sup>38</sup> With this point we enter into the organic contribution made by the legislature. Of equal importance in this realm is the non-technical character of the legislature.<sup>39</sup> The legislature brings to the enactment process the intangible qualities of the non-expert, the insights and sensitivities of the non-technical mind. To be sure, the top political portions of the executive make a similar qualitative contribution. But bureaucracy tends to envelop and

<sup>37</sup> C. J. Friedrich, *Constitutional Government and Democracy* (Boston, Ginn and Company, 1950), Chap. 16.

<sup>38</sup> Elaine Tanner, *The Function of the Modern Legislature* (Radcliffe College, unpublished manuscript, 1950).

<sup>39</sup> *Ibid.*

ossify its masters and, therefore, the vindication of the obvious falls most often to the legislature. We may conclude, then, that popular control over the enactment of law is best served when the executive is the originating, directing and unifying force, and the legislature functions to criticize and control on behalf of the nation.

The same holds true in execution. The President and his administrative chiefs must be in charge of the whole administrative process subject, of course, to the criticism of the legislature. The premise of constitutionalism has always been that bureaucracy suffers from an inherent tendency to decay toward that formalism and parochialism which ruin efficiency and toward that aggrandizement on the part of officials which destroys responsibility. The political executive, the top-level policy agents of the President, though a necessary and desirable means of fighting these tendencies, cannot be relied upon completely. Too often these men become mere captives of their departments both because of their own lack of information, time and expertise as contrasted with their subordinates' expertise, persistence and command of facts, and because of the psychological effects of having continually to act as the spokesmen for and defenders of the department's interests. Legislative oversight constitutes a vitally needed safeguard functionally and qualitatively.<sup>40</sup> It adds the additional brake which guarantees the capacity of the people to call the bureaucracy to account.

Nevertheless, the legislature must not exercise its control in such a way as to disrupt Presidential leadership of the administrative process. Congress must criticize, but it must not seek to subvert the President's ability to steer and manage the vast number of executive departments and agencies in the complex

<sup>40</sup> Review by courts and professional responsibility (the inner check) are also essential and desirable means of controlling administration. However, neither of these obviates the necessity for legislative oversight. True, in the modern state much must be left to the conscience of the administrative official. Yet constitutionalism requires that this be encased within the boundaries delimited by checks of a more tangible and coercive nature. For constitutionalism professional responsibility is never enough. The importance of holding the bureaucracy accountable to some other body does not decrease even in the face of a high degree of subjective control. The protection provided by courts is purely negative and *post hoc*. Courts can only provide a remedy if it can be established that administrators have abused their discretion, overstepped their jurisdiction, or committed an error of law, fact, or procedure. But they cannot safeguard the public against red-tape, offensive conduct, or failure to act.



business of carrying out the law. The President must be allowed to retain primary responsibility for the direction of the bureaucracy.

Legislative leadership in the administrative process tends to atomize administrative structure and to deliver it into the hands of the entrenched minorities in the committees. Administrative agencies by nature tend toward particularism and conflict, especially if organized on a clientele basis. If integration is to occur, it must be imposed on them from above. Yet, as in enactment, the legislature is unable to organize itself to provide for central and coherent direction. Thus, the typical results of legislative direction usually prove disastrous for the proper functioning of the constitutional democratic state. On the one hand, administrative responsibility for policy proposals is rendered meaningless. Legislators must have balanced programs placed before them if they are to be able to make intelligent policy decisions. When presented with uncoordinated policy proposals, the legislative mind is confused and its decisions are necessarily irrational. On the other hand, the legislature's ability to hold the administration accountable for policy and performance is vitiated. With regard to policy accountability requires a coherent program over which and in terms of which control can be exercised. Unless such integration exists, control is devoid of significance. For then the legislature finds itself in the ridiculous position of holding different agencies accountable for conflicting policy. With regard to performance the negation of Presidential leadership impairs the coordinated management of current operations. If the legislature is vested with direction of the administrative process, one is likely to get the type of situation in which one agency frustrates the work of another.

In summary, the proper roles of the executive and legislative branches are as follows: Prenatally, i.e., before the enactment of a statute, the executive should present well-balanced legislative proposals which focus on major issues and meet the demands of the hour. The job of the legislature is to refine these proposals into even closer harmony with community demands. Postnatally, i.e., after the enactment of a statute, the executive must implement the statute both responsibly and efficiently. The point with regard to postnatal responsibility is not com-



plex. The idea is that policy decisions made by the executive in the implementation of a statute must be calculated to accord with the letter and spirit of the act. The point with regard to efficiency is more subtle for efficiency has both a substantive and a procedural sense. Substantively, the idea is that policy decisions though responsible may vary in the extent to which they actually contribute to the realization of the purposes of a statute. Procedurally, efficiency refers to the manner in which policy is carried out operationally. Inefficient performance may frustrate effective implementation of a law just as efficaciously as irresponsibility or substantive inefficiency. Hence, the role of the legislature is both to insure policy responsibility and efficiency, and to prevent waste, corruption, red-tape, officiousness, etc. That is, to hold the bureaucracy accountable for policy and performance.

As indicated above, this is not to say that policy and performance can ever be compartmentalized. Obviously, the process of execution is an inextricable mixture of discretion and operation. It is only to say that legislative control will never be complete unless it checks bureaucracy with regard to both policy and performance. The difference is necessarily one of emphasis and approach. But such a difference is still very significant. Congress must take pains to insure that its control is framed in terms of a dual emphasis on both the substance of implementing policy decisions and the manner of administrative operation. Its instruments of control must operate on two overlapping but distinct lines of approach in order to account for both aspects of execution. For although policy and performance exist as an intermingled whole, and although any complete judgment must take both into account, still to some extent each one must be considered, approached, and understood separately.

*Principles of Executive-Legislative Relations.* If these are the proper roles of the respective branches, what principles can be deduced from them to guide the ordering of their relations? Two maxims are immediately apparent.<sup>41</sup> First, the legislature should concentrate on broad policy and general administrative performance. This contention can be supported both func-

<sup>41</sup> A. A. Maass, *Muddy Waters* (Cambridge, Harvard University Press, 1951), p. 8.

tionally and qualitatively. In terms of the Tanner approach the unspecialized mind of the legislature is most effectively utilized when it treats broad policy proposals, broad administrative policy decisions and general administrative performance rather than the details of policy or administration.<sup>42</sup> In terms of the needs of popular control over enactment and execution the case is equally as clear. In enactment, the sheer quantity of work to be done means that proper selectivity is essential for effective functioning. Assuming that the legislature wishes to serve as a potent weapon for criticism and control on behalf of the nation, it has no choice but to focus on the great issues of policy and to rest content with laying down general lines of policy for the executive branch to follow. In addition, postnatal policy control requires that the legislature concentrate on broad policy prenationally. For the effectiveness of postnatal policy accountability depends on the existence of clearly defined statutory policy standards, and as a result the legislature must hold the administration accountable for pointing up broad policy questions and playing down details so that such standards can be formulated. Lastly, unless the legislature concentrates on broad policy in the enactment process, subsequent administration is likely to be impeded. Detailed statutes either hamper administration *per se* or hamper it indirectly by forcing administrators to commute continually to and from Capitol Hill in order to secure approval for their actions.

Similarly in the process of execution neither accountability for policy decisions nor accountability for administrative efficiency is served by legislative concentration on detail. Here again the sheer amount of work to be done makes proper selection essential to adequate control. With regard to administrative performance legislative concern with detail does not insure efficiency since efficiency has to be evaluated in terms of the total operation of a department or agency. Indeed, legislative concentration on detail is more likely to result in inefficiency since it induces administrative officials to multiply red-tape in order to avoid mistakes and to be overly cautious. With regard to policy it has already been pointed out that bureaucracy is

<sup>42</sup> Tanner, *op. cit.*

held accountable for responsible and efficient policy decisions most effectively through reliance on broad policy standards.

The second maxim that the legislature should adopt as a guide to ordering its relations with the bureaucracy is that of indirect accountability. That is to say, it should hold the bureaucracy accountable through the Chief Executive, not in a direct manner. This maxim is merely a formulation of what was stated above with respect to the necessities of Presidential leadership. In other words, the fundamental aim of the maxim is the achievement of unified direction of the executive functions of government in order that such cohesion may serve as a prop not only for executive leadership in enactment and execution but also for legislative criticism and control of broad policy and performance.

*Problems of Practicality.* Given such roles and principles, one cannot escape the conclusion that Congress has paid too little attention to structuring and using the veto in ways calculated to provide for these considerations. With regard to performance the veto has been used to review such matters as military real estate transactions, military construction projects, lease-purchase programs, small watershed projects, airport construction projects, rent adjustment in Federal housing for Governmental employees, concession contracts for the National Parks, irrigation repayment contracts, naval petroleum contracts, surplus property disposals and synthetic rubber plant disposals.<sup>43</sup> But of all these utilizations only the latter two meet the requirements of general performance control. With respect to policy the veto has been used to review such matters as reorganization plans, deportation suspension orders, permanent residence grants for certain kinds of aliens, atomic energy production licenses, atomic information exchange agreements, electric utility contracts negotiated by the Atomic Energy Commission, disposals of Defense Department production facilities, disposals of World War II surplus property, and disposals of rubber plant facilities. However, those utilizations concerned with deportation suspension orders and permanent residence grants constitute almost 33 per cent of all policy di-

<sup>43</sup> Veto review of petroleum contracts was contained in 58 Stat. 281 (1944).

rected veto utilizations, and the status of these areas as broad policy areas is highly debatable.<sup>44</sup>

To be sure, this is not to say that the veto has not made significant contributions in certain areas of policy or to say that some type of performance control is not needed in those areas in which the veto has been used. Moreover, in many respects the veto has come as a definite improvement over past procedures. A good illustration is the Lease-Purchase Act of 1954 which broadens the scope and reach of the Government's public building programs.<sup>45</sup> The point simply is that on the whole Congress has been overly concerned with the necessities of the immediate moment and that as a result it has not used or structured the veto in such a manner as would best contribute to its role as critic and controller on behalf of the nation.

Only on this basis can we adequately account for the diverse fates of various veto bills. For instance, veto review of the projects of the Housing and Home Finance Agency was struck down on a point of order as legislation in an appropriations bill. Yet veto review of production facility disposals by the Department of Defense was also tacked on to an appropriations bill and it went through unscathed. To understand this apparent incongruity we have simply to look at some of the comments

<sup>44</sup> The Alien Registration Act of 1940 authorized the Attorney-General to suspend the deportation of aliens in those cases where deportation would cause serious economic harm to a citizen or legally resident alien. However all orders involving a suspension of six months or more were required to lie before the Congress for a whole session subject to disallowance by concurrent resolution at any time within that period (P.L. 670, 76th Cong., 2nd Sess.). In 1948 the Act was amended to require affirmative approval for all such orders within six months after their issuance (62 Stat. 1206).

The Immigrant and Nationalities Act of 1952 embodies the two-House negative form for reviewing deportation suspensions of certain types of aliens and the two-House affirmative form for reviewing deportation suspensions of other types of aliens (66 Stat. 216). This act is essentially a compromise between the veto provisions of the Alien Registration Acts of 1940 and 1948. The Displaced Persons Act of 1948 and the Refugee Relief Act of 1953 applied the same procedure to displaced persons and refugees from Iron Curtain Countries. Both acts, in addition to admitting a large number of persons into the United States, stipulate that persons already resident in the United States who fall under the jurisdiction of the acts can be granted permanent residence status upon recommendation by the Attorney-General and approval by both Houses of Congress. (62 Stat. 1011 and P.L. 203, 83rd Cong., 1st Sess.)

<sup>45</sup> This act permits the Postmaster General and the General Services Administration to acquire title to existing buildings and buildings constructed for purposes of subsequent lease-purchase by applying annual rental payments against the purchase price, provided that no appropriation can be made for projects not approved by the House and Senate Public Works Committees. (P.L. 519, 83rd Congress, 2nd Session.)

made on the floor of Congress. Speaking in opposition to the Housing veto, Representative Garmatz (D., Md.) ably summed up the feeling of Congress, "The point is that this rider appears to be intended to place a new roadblock in the way of an effective housing program. . . ." <sup>46</sup> In short, one of the main objections to the Housing veto was that it would interfere with projects that each Congressman wanted. With regard to the Defense veto a comment made by Representative Vinson (D., Ga.) is illustrative. In reply to a jibe that his opposition to the veto was "off the beam," he caustically remarked, "I suppose I would be on the beam if I had a Navy Yard in my district." <sup>47</sup>

Similarly, Congress' failure to profit fully from the lessons contained in the past history of the veto becomes explicable only when we recognize the extent to which it has been governed by instant needs and short-run considerations. Structurally, there has been a proliferation of forms with no real attempt to limit, systematize, and arrange these forms in terms of their respective advantages and disadvantages in various fields of veto endeavor. A good example is the waiting-period form. Two different types of waiting-periods have been used. In one the veto bill itself designates the committees which are to pass on the executive proposals. In the other the veto bill leaves the choice to the discretion of the Congress. This difference is not a superficial one since the exigencies of democracy demand that the veto be used as an instrument for control by the whole Congress. The important committees of the Congress are the bailiwicks of the special interests and the members of Congress who represent districts of extreme single party domination. To give these strategically placed minorities legal control over the veto is to vitiate the ability of legislative majorities to command the legislative process and to oversee the workings of the bureaucracy. Waiting-period forms which stipulate that executive actions are to lie before the whole Congress rather than before specific committees vest legal control of the veto in the whole Congress, where it belongs, and in so doing preserve Congress' ability to have the last say, give it the advantages that flexibility in choice inevitably bring,

<sup>46</sup> 101 Cong. Rec. 3352 (Unbound, March 30, 1955).

<sup>47</sup> 101 Cong. Rec. 5307 (Unbound, May 12, 1955).

and induce individual Congressmen to regard the area under veto review as an area within the sphere of their legitimate concern rather than an area over which entrenched minorities in the committees have exclusive prerogatives. However, Congress has not taken pains to preserve its legal control in one out of every three veto acts which have utilized the waiting-period mechanism.<sup>48</sup>

Employment-wise, Congress has failed to develop and elaborate those potentialities of the veto which are most relevant to the broader problems that confront all modern legislatures. In an industrial age continually growing more complex Congress faces the necessity of delegating more and more of its authority and discretion to the executive. Yet, under its present system of oversight controls, to delegate the requisite amount of discretion and authority in certain important areas of legislative endeavor may very well be to lose all subsequent influence in the area. Consequently, in many instances the only alternatives before the Congress are obstruction or impotence. It may delegate power without provision for hamstringing the executive even though this involves renunciation of future control; it may refuse to delegate power even though this involves neglecting a positive need for substantive action; or it may delegate the power under conditions that strangle administrative flexibility and workability.

For this reason it is essential that Congress devise new weapons of accountability, weapons designed to meet the demands of a modern age. Thus far, Congress has not comprehensively approached the veto from this point of view. Instead, it has largely ignored the lines of suggestion implicit in such measures as the Atomic Energy Act of 1946 and the Rubber Producing Facilities Disposal Act of 1953. What is needed now is an approach which will correct this myopia, an approach based on that higher kind of pragmatism which emphasizes the broad ends and needs of democratic government rather than the narrow and limiting practicality of the immediate moment.

<sup>48</sup> Formal control has been vested in specific committees with regard to irrigation repayment contract, electric utility contracts negotiated by the A.E.C., and international atomic information exchange agreements (the Atomic Energy Act of 1954). On the other hand, the Surplus Property Act of 1944, the Atomic Energy Act of 1946, the Interior Department Appropriation Act of 1953 (concession contracts for the National Parks) and the Small Watershed Act of 1954 vest formal control in the Congress.



This essay is an attempt at such an approach. It is an attempt to apply institutional principles and past experience to the veto in order both to sketch out some guidelines for its use and structure and to indicate the extent of its possible contribution if properly structured and used.

#### PROPER SPHERE OF OPERATION

The veto like all other devices of Congressional control should be confined within the realm of broad policy and general administrative performance. Here, as elsewhere, the key to effective use of the device is proper circumscription and proper selection. The results of indiscriminate veto control would be to entangle Congress and its committees in such a web of details as to lose the advantages of delegation and the possibility of oversight over the broader aspects of policy and performance. In addition, detailed review dampens enthusiasm for the whole job of review.

Of equal importance as a reason for rejecting detailed control is the fact that such control places the veto in the hands of the committees rather than in the hands of the whole Congress. Either officially or unofficially the committees become the wielders of the veto. For even if a statute formally required action by the Congress, such action would become a mere fiction in the preponderant number of cases. The individual members of Congress would have neither the time nor the skill to pass on the vast volume of material placed before them. They would be forced to defer to committee recommendations. In other words, practical as well as legal control of the veto by the committees inhibits its use as an instrument for control by the whole Congress.

*Detail and the Veto.* All this is not to say that any use of the veto which involves an extended review of a mass of material is necessarily an instance of detailed review. Broad policy or performance review is always a function of the object of the review and the data involved and must be evaluated primarily in these terms rather than primarily in quantitative terms of size and number.

What we must not forget is that while nature makes size and number, only man finds or creates meaning. Detail is always a compound of three interrelated variables: context,



degree, and subjective valuation. Areas of policy or performance gain significance, become broad or general, principally because they are seen as vital in terms of some value system, not because of their inherent properties. Similarly, data within these areas gain significance out of the character of their relationship to the area. Thus, detail is a formal rather than a substantive concept. There is no common quality to detail that can be identified precisely, abstracted concretely, or applied universally. Instead, the only characteristic that details share in all their manifestations is a common and similar relation to their contexts or environs—they are unimportant. Of course, even within definite contexts the significance or insignificance of a matter cannot be proven with demonstrative certainty. Nevertheless, argument can still be meaningful and decision can still be objective. For given a commonly accepted value or a commonly accepted area recognized as broad in terms of some commonly accepted value, reason and experience can supply "contingent" knowledge with regard to what constitutes detail in terms of areas and with regard to what constitutes detail within broad areas.

Nor does the disregard of detail demand the disregard of basic data. Accountability for policy and performance cannot exist in a vacuum. Both need a concrete foundation in fact since it is only through the use of facts, small and large, that accountability can be instituted. The point implicit in the maxim of broad accountability is not that basic data should be neglected but that it should be put in proper perspective, not that it should be ignored but that the right kind should be chosen and utilized in such a way as to effect broad accountability for policy and performance. For example, information with regard to how much the Post Office Department spent on pencils probably would not be particularly helpful in the evaluation of general administrative performance. But mail route service statistics might very well be indicative.

Applying these ideas to the veto, if the object of the review is a broad policy or performance problem and if the data involved serves as a practical and highly relevant handle with which to get at the object, then veto review should not be struck down on the issue of detailedness even though the quantitative demands of such review are considerable. A good illus-

tration is Section 638 of the Defense Appropriation Act of 1956. On the surface this appears as a most malicious example of detailed review. Yet a good case can be made for the opposite view. Congress, though in favor of the general proposition of getting Government out of business, did not want disposals to take place where such disposals would be unsound, unfeasible, uneconomic, or not in accord with the needs of national defense.<sup>49</sup> Consequently, it can be argued that Congress was justified in instituting review over the very disposals in order to insure that a business-oriented Administration did not dispose of facilities indiscriminately merely to serve its own ideological and practical interests.

On the other hand, some qualifications are necessary. The most likely result of use of the veto in areas which require an extended examination of multitudinous materials is detailed review. Though cases such as Section 638 are not infrequent, they are nevertheless exceptions and they exist as exceptions in part at least because they fall within reasonable quantitative bounds. Those instances in which the veto could properly be applied for extended review of a vast mass of data will necessarily be few and far between. For example, most areas of administrative rule-making must remain free of veto control. For though the relevancy of data depends on its inner as well as its outer features, still the most highly relevant data is probably not to be gained from a perusal of the myriads of administrative functionings. Though there is no one-to-one relationship between quantity and quality, still the two tend to go together. Again, this is not to say that quality can never withstand the dilution effected by extensive division in terms of size and number; it is only to say that the intrinsic nature of the object and the data have to be of great significance for it to do so, and that, therefore, such instances are not everyday occurrences.

In truth, the smaller a fact is the less likely it is to be important. Etymologically, the root of the word detail means to cut or chop apart, and truly those matters which are most chopped up are most likely to be details. For example, veto review of concession contracts for the National Parks seems to this writer to constitute detailed review. Of course, the rele-

<sup>49</sup> 101 Cong. Rec. 7423 (Unbound, June 20, 1955).

vancy of data is a matter of degree, but concession contracts are not so indicative of general departmental efficiency as to justify such close scrutiny. Checking them through the veto allows the facts to become ends in themselves instead of means for focusing on broad performance.

Moreover, the more numerous the body of data the less likely is broad control. Broad control depends on the utility of the data as well as its indicative quality, though, of course, the two are related. To illustrate, veto review of the Attorney-General's deportation suspension orders seems to this writer to be a mistake. The number of such orders is just too enormous to permit effective review. And it is a delusion to think that the mere provision for affirmation or non-negation of these orders constitutes much of an improvement over no review at all when in the vast majority of cases such action is undiscerning and automatic. To be sure, some would argue that the virtue in such an approach is that it allows objections to be raised when they do occur. But assuming that deportation suspension policy is an important policy area, would it not be better to concentrate on the broader aspects of such policy rather than blindly and haphazardly striking down some of its manifestations?

The answer is not clear-cut. In a few vitally significant areas of policy where the veto presents itself as the only effective means of control there may be some justification for this shotgun approach despite its many limitations in practice and in democratic theory. In such areas haphazard review of minutiae may still be preferable to no review at all, especially if the nature of the policy involved is such that the committees are likely to act for the whole Congress instead of for their own special interests. Thus, the desirability of veto review of alien deportation suspension orders remains an open question depending on one's view of the significance of this area of policy and the efficacy of other means of control. Yet, generally, the body of data under veto review must not be so voluminous as to render Congress incapable of dealing with it. Nor must the body of data under veto review involve such a myriad of matters as to give practical control of the veto to the committees, though in most such cases it is even questionable whether committees can give more than perfunctory ap-

proval.<sup>50</sup> In short, in the preponderant number of cases veto review can only involve the review of numerous rather than voluminous data if it is not to be detailed review. This distinction is somewhat rough, but it is well illustrated by the difference between veto review of contracts disposing of the Government's synthetic rubber plants and the unsuccessful attempt at veto review of public housing, slum clearance and urban renewal projects.<sup>51</sup> In the former instance the number of disposals was not so great as to vitiate Congress's ability for effective review or to vest committees with practical control. In the latter instance not only was committee control required, it was even doubtful whether the committees could effectively exercise such control since review here involved more than 2000 clearances annually. Said House Banking Committee Chairman Brent Spence (D., Ky.), "The Appropriations Committee has usurped the functions and invaded the jurisdiction of the Banking and Currency Committee in trying to give it authority it doesn't want and couldn't administer."<sup>52</sup>

*Policy and the Veto.* However, it is not desirable to blanket administration with the veto even in those instances where such review does satisfy the exigencies of broad control. The criterion of broad policy and performance sets only an outer boundary for proper use of the veto. Further delimitations in the sphere of the veto must be made through placing the veto in proper perspective with regard to the other weapons in the Congressional arsenal. That is, we must identify those areas of decision-making and performance for which the veto is better qualified to serve as an instrument of control than are such traditional means as appropriations, investigations, reports, the audit, legislation, removal of personnel, criticism on the floor, etc.

Remembering the overlapping distinction we made between policy and performance, let us approach the problem of further delineation in these terms. Policy-wise, as a general rule, Congress should give decision-making power to the executive in those instances where it is not qualified to decide the matter, where the executive is particularly better suited to decide the

<sup>50</sup> Editors, "Laying on the Table," *Harvard Law Review*, February 1952, p. 643.

<sup>51</sup> H.R. 5240, 84th Cong., 1st Sess.

<sup>52</sup> *Washington Post and Times Herald*, March 30, 1955.

matter, or where it itself is unwilling to decide the matter though the matter is pressing. But in certain areas of policy the "normal" means of Congressional control over executive discretion fall far short of insuring an adequate degree of accountability. On many occasions standards cannot be clearly or meaningfully defined in a statute. For example, the exigencies of flexibility may repel any but the broadest types of standards. As Justice Cardozo put it, speaking with regard to the standard of "ordinary and necessary expenses" contained in the Revenue Acts, "The standard set up by the statute is not a rule of law; it is rather a way of life. Life in all its fullness must supply the answer to the riddle."<sup>53</sup> Or Congress itself may not be competent to set definite standards. This may be due to its inherent limitations as a body of laymen or to the fact that a particular area is relatively unexplored and, hence, not clearly understood. In some of the New Deal statutes the delegation was not much more explicit than a direction to deal with the situation, be it the demoralization of industry or farming. Moreover, with regard to certain types of executive discretion even adequate prescription of the pattern and limits of delegation may not provide for adequate control. For example, take the anti-monopoly standard contained in the Surplus Property Act of 1944. Suppose Congress had felt that the disposal policies of the Surplus Property Board fostered monopoly, what could it have done through its regular means of control? Here even the potent weapon of appropriations was likely to be ineffective since the Board would require the same appropriation to carry on its operations no matter how it exercised its decision-making power.<sup>54</sup> In other words, adequate control in this situation as well as in both of the above situations demands not only a check on action but a check on the very authorization of action. This only the veto can provide.

In addition, in other areas of policy political stalemates in the legislature often prevent affirmative action. Nevertheless the Congress will not delegate these decisions outright if it feels them of such a significant nature as to necessitate legisla-

<sup>53</sup> *Welch v. Helvering*, 290 U. S. 111 (1933).

<sup>54</sup> Congress could, of course, revise or tighten the legislative standards of the Disposal Act. However, what must be remembered is that any attempt to tie down standards too precisely impairs administrative flexibility and workability.

tive participation in their actual determination rather than mere oversight "after the fact." Here, too, the possibility of veto review offers a means of reconciliation. The Reorganization Act of 1939 is a good case in point. Until 1939 obstructive minorities in the legislature had succeeded in preventing badly needed reorganization of certain agencies and functions within the executive branch. What the Reorganization Act of 1939 did was both to induce Congress to delegate the power and to turn the tables on the minorities. For the possibility of negation by concurrent resolution satisfied the requirements of Congressional potency while simultaneously placing the minorities in the unenviable position of having to muster a majority of both Houses to save their pet agencies.

This is not to say that the veto should be used in all cases where minority obstruction produces legislative stalemates. Some decisions are so basic and significant that they must not be given to the executive. In these most basic phases of policy the legislature has to take responsibility for resolving its own dilemmas. Democracy requires that the broadest and most vital matters be decided in the legislative process since this is the arena in which the elected representatives of the community, Presidential and Congressional, participate. The point rather involves those areas of policy stalemate which are broad but not too broad to be delegated to the executive if veto review is included. This distinction is very tenuous theoretically, but practically there is no problem. Congress is neither disposed nor required to give up the broadest areas of decision-making to the executive. On the whole Congress is both willing and able to settle the broadest matters of policy even when considerable expertise is required. The executive has no monopoly on intelligence. For over a century Congress wrote every provision in the tariff laws and it now practically rewrites the highly complex farm bills offered by each Administration. The maxim of broad accountability does not derive from Congress' inherent inability to examine details. Congress' legislative staffs presently possess high expertise and could be improved to the extent necessary to provide the level of expertise now lacking. The maxim derives instead from the fact that time is limited, duplication wasteful, and Congressional control most effective functionally and qualitatively



when it concentrates on the broader aspects of policy and performance. In those cases in which the Congress cannot resolve most basic issues delegation to the executive is made only at the expense of the exigencies of democracy even if veto review is included.

In conclusion, the most proper area for veto operation with respect to policy is what might be called the middle-ground area of decision-making. That is, the area of decision-making in which the traditional means of control now offer the Congress only a choice between obstruction or impotence.<sup>55</sup> Accepting this, the sphere of the veto's policy operation can be delimited primarily in terms of two concentric circles. The outer boundary line should be drawn in relation to the notion of broad policy accountability; the inner boundary line should be drawn as a function of the notion of middle-ground operation. Of secondary importance is the veto's use in areas which are now adequately controlled but for which the veto offers a more sensitive means of control. But if the veto is so used, care should be taken to insure that there is proper correlation between subject-matter and form of regulation. For the danger exists that the veto will be over-extended to matters which can be controlled more efficiently through more flexible instruments and to matters which do not require such close control.

*Performance and the Veto.* As is evident from the fact that only two of the many performance-directed uses of the veto satisfy the criterion of broad accountability, the veto is not well adapted for use in the field of performance. Both because of its own inherent qualities and because of the nature of the operational aspect of administration, the veto tends toward emphasis on detail. The problem is that in order to be implemented the veto has to be tied on to something. When the veto is directed to policy, it often is relatively easy to attach it to data which can serve as a convenient handle for approaching broad policy issues. Conversely, when the veto is directed to operations the only hitching posts are usually isolated details.

For the most part the indicative qualities of specific actions in the field of performance are rather low. A veto can check a particular contract negotiated by the Secretary of Agriculture,

<sup>55</sup> The notion of a middle-ground area of policy is derived in large part from Peter Schaufler. See his unpublished Ph.D. thesis on the veto (Harvard).



but it is hard put to find specific actions through which the Department's general efficiency can be checked.<sup>56</sup> To be effective in this regard a device must have breadth and freedom. It must be able to range over all phases of administrative operations in a field finding its subject-matter at random as it appears significant. For that reason committee hearings or investigations when supported by the weapon of appropriations are perhaps the best means of general performance control. A good illustration of their efficacy as a means for broad performance control is their use with respect to the construction, purchase and lease of reserve armories.<sup>57</sup> Here, though the Defense Department requested an initial outlay of over a billion dollars, Congress authorized the appropriation of only \$250 million and required the Defense Department to make continuing reports on the progress of the program. At the end of five years the Department had to come back to Congress for additional authorization, and hearings were held which reviewed the general accomplishments and efficiency of the program up to that time.<sup>58</sup>

Thus, the veto should not be employed to check administrative performance since the veto is not likely to serve as an instrument for broad control and since other instruments of Congressional control are better suited for the job. The task of holding administration accountable for general administrative performance usually requires a type of flexibility that the veto just does not have. But some exceptions can be made. At times veto review may satisfy the exigencies of general performance control and middle-ground operation. A notable example is the Rubber Producing Facilities Disposal Act of

<sup>56</sup> This is not to say that the checking of a contract is always an instance of performance rather than policy review. Note the Rubber Producing Facilities Disposal Act of 1953. Here one of the main reasons for subjecting the report to a one-House veto was to insure that adequate provision was made for a competitive synthetic rubber industry (99 Cong. Rec. 9362). Thus, it must be remembered that the type of accountability emphasized cannot always be discerned from the type of action checked. Instead, one must look behind the action to see if it is being checked primarily for purposes of insuring policy responsibility or for purposes of insuring administrative efficiency. Indeed, one veto could do both in the right kind of situation. Again, note the Rubber Producing Facilities Disposal Act of 1953. The disposal plan was checked not only to insure policy responsibility, but also to insure that the government got a fair return on the sale. For the plants cost the government over \$500 million.

<sup>57</sup> National Defense Facilities Act of 1950, P.L. 783, 80th Cong., 2nd Sess.

<sup>58</sup> H.R. 2107, 84th Cong., 1st Sess.

1953. Here the data involved were highly relevant for a general performance problem, i.e., insuring the Government a fair return on the sale, and the veto was the most effective means of overseeing the disposals as breach of contract was involved. In addition, if an instance of administrative performance is so significant as to justify examination of the data on its own merits, it may be all right to institute veto review, especially if other means of control are lacking. Indeed, in performance there is even a stronger case for such review than in policy since the disadvantages of control by committees are mitigated by the fact that the special interests of the committees, e.g., efficiency, economy, etc., are likely to correspond to the desires of the whole Congress. Of course, great dangers are still involved, but this shotgun approach may be acceptably be a proper utilization of the veto in a limited number of cases and it is, therefore, desirable in performance as well as in policy to apply the proposals for veto review individually and pragmatically. The veto might possibly be utilized as a disciplinary weapon over especially wayward administrators when dismissal is neither practical nor desirable.

#### PROPER STRUCTURE

But merely knowing how to use the veto is not enough. Improper structuring of the device vitiates its advantages and dilutes its potential contribution. Obviously, we must also know how to structure the device if we are to use it most effectively.

*Forms of Expression.* If the device is to be used to the greatest possible advantage, committee control, affirmative approval, and amendability must be excluded.

As an absolute rule, legal powers of control over the veto must not be vested in committees. As a general rule, practical control of the veto by committees should be avoided. Our previous discussion has already touched on the main reasons for such working biases. To this we need simply to add the following addendum: subjecting the veto to committee control can mutilate the very essence of the veto. One of its integral features is its facility in hurdling the barriers which powerful special interests set up to majority control of the legislature. To vest the veto in committees then may well be to take away

with the left hand what has been granted with the right. For example, how successful would the Reorganization Act of 1939 have been if committee approval had been stipulated?

Yet to say that committees should not be vested with control of the veto is not to say that committees do not have a definite and significant role to play in implementing veto review. Measures subject to veto review have to be referred to standing committees familiar with the field, the intent of Congress, and the department whose proposals are in question if there is to be a basis for effective and intelligent discussion on the floor of Congress.<sup>59</sup> The point is merely that though Congress cannot hold the administration accountable without the information and expertise that its committees provide, still committees must never be allowed to become the masters rather than the servants of Congress. Instead of becoming ends in themselves, committees should serve either as instruments for implementing veto review by the whole Congress or in a minority of cases as the agents of Congress in veto review. Excluding the limited number of exceptions in which committee review on behalf of Congress is justifiable, committees must not be vested with determinate powers of decision over the veto any more than they would be vested with determinate powers of decision over regular legislation or appropriations. Forms of the veto such as the Small Watershed Act of 1954 or the Naval Land Transfer Act of 1944, which subject contracts negotiated by administrative agencies to final approval by committees, are, in the opinion of this writer, misconstructions of the device.<sup>60</sup>

The case against including affirmative approval and amendability as features of the veto device is in many ways similar to the case against the committee-action form. Again, the point is that provisions which subject proposals to amendment

<sup>59</sup> Congress' regular specialized committees are to be preferred over the establishment of one committee for the sole purpose of veto review. The range and number of measures that can be subject to veto review, even with the limitations of broad policy accountability, would render one large committee ineffective unless it divided itself into specialized departments. But this would be mere duplication since such specialized departments already exist in the regular committee structure.

<sup>60</sup> A more subtle form of vesting the veto in committees is illustrated by certain laws which require the G.S.A. to report to committees prospective acquisitions and dispositions of most kinds of real property and all kinds of surplus property (P.L. 152, 81st Cong. and P.L. 522, 82nd Cong.). These Committees have used the reports as a bludgeon for close control in this regard knowing full well that its expressions of disapproval serve to intimidate the agency. See the proud boasts of Rep. Carl Vinson (D., Ga.) (97 Cong. Rec. 4187).

or affirmative approval stabilize the power of entrenched minorities. With regard to the latter unless proposals made under the device are effective if not negated rather than ineffective if not approved, the veto may not serve as a means for subjecting a field of administration to control by the whole Congress, and it certainly will not serve as a means for escaping deadlocks caused by minority squabbings. The potency of the veto in both regards lies to a large extent in the fact that the feature of negation isolates and weakens the special interests. In the regular legislative process the field is wide open for all the tactics of log-rolling, obstruction, and delay for which the special interest groups are so justly famed. However, under the negative form strategic advantage is placed with the majorities. Members who would hesitate or even refuse to cast a positive vote of approval might, on the other hand, be willing to refrain from voting disapproval. More important, since proposals go into effect unless negated, the burden of effort is placed on the minorities. Whereas formerly they could merely obstruct, under the negative form they have to organize sufficient support to strike down the measures. This will be no mean achievement even for the most skillful log-rollers in Congress. On the other hand, if negation resolutions are made privileged, real majorities will have no trouble expressing themselves.

None of these advantages accrue to the affirmative form of the veto. Practically, there is no difference between regular legislative action on a presidential recommendation and affirmative approval under the veto device. In 1939 when proponents of the affirmative form pressed their case, John McCormack (D., Mass.) wisely replied, ". . . you and I, as practical men, know that if the President sends up recommendations with reference to reorganization . . . the Congress would not pass the necessary enabling resolutions."<sup>61</sup> In 1949, in debate over the Reorganization Act of that year, Rep. Chet Holifield (D., Calif.) made the same point, ". . . the fact remains that every attempt on the part of Congress to take affirmative action . . . has miserably failed."<sup>62</sup> In short, the affirmative form of the veto in no way strengthens the cause of representative control. It comes as no improvement over the regular legislative process

<sup>61</sup> 84 Cong. Rec. 2414.

<sup>62</sup> 95 Cong. Rec. 892.

because it in no way more effectively limits the power of the entrenched minorities.

As for amendability the content of the executive's proposals must remain inviolate. For, again, unless non-amendability is stipulated, a majority expression will not be assured.<sup>63</sup> In the words of Peter Schauffler,

The legislative veto (with non-amendability) has the result of promoting an automatic and expeditious alignment for or against an executive proposal . . . by all the affected interests playing upon the Congress. It produces a carefully scheduled Congressional expression of only the resultant of those forces. The idiosyncrasies of amendment and procrastination so often typical of committee consideration and floor management are avoided, . . . (and) . . . a true indication of total Congressional sentiment on the total content of any plans which are permitted to take effect (is assured).<sup>64</sup>

In the regular legislative process unrestricted amendability is permissible since ultimately the executive can protect the coherence of his program through the Presidential veto. But, under the legislative veto system the legislative process is reversed. If unrestricted amendability were permitted, the President would become a mere figurehead. The Congress could wreak havoc with his proposals without fear of disciplinary action through the Presidential veto, and these proposals would be effected in exactly the mutilated form in which they emerged from the Congress. For this reason the exigencies of balanced and integrated policy require that executive proposals made under the veto device should not be subject to amendment.

Nevertheless, ways of softening non-amendability should be explored in order to make the veto more flexible.<sup>65</sup> At present, the item veto and the separate package arrangement present themselves as the most likely candidates for such a purpose. Under the separate package arrangement the content of particular executive proposals is restricted to matters which involve single discrete program units.<sup>66</sup> In most cases this is to be

<sup>63</sup> Peter Schauffler, Draft of Ph.D. Thesis on Legislative Veto (Harvard University), Introduction, pp. 2-3.

<sup>64</sup> *Ibid.*, p. 2.

<sup>65</sup> *Ibid.*, p. 64.

<sup>66</sup> *Ibid.*, p. 64.

preferred over the item veto. In those instances in which reliance on the item veto is contemplated care should be taken to foresee the possible distortions such a veto could effect. If its use can conceivably alter the original character of an executive proposal, it should not be instituted. Furthermore, neither the item veto nor the separate package arrangement should be instituted if they measurably strengthen the influence of minorities. To this extent flexibility must continue to suffer. Thus, there is little to be said for wrapping the separate package requirement around any proposed reorganization of the Corps of Engineers unless, of course, it is done as a matter of expediency to secure the passage of a general reorganization act. A good illustration of the proper use of softening mechanisms is the Rubber Producing Facilities Disposal Act of 1953. Here an item veto gave Congress an opportunity to look at every one of the disposals freeing it from the necessity of passing on a cumulative group of sales in one fell swoop.

In summation, the following can be concluded with regard to the manner in which the veto should be expressed. First, proposals under veto review should not be subject to amendment. Second, proposals subject to veto review should take effect unless negated. Third, the device should be limited to the one-House veto, i.e., proposals go into effect unless negated by either House of Congress, the two-House veto, i.e., proposals go into effect unless negated by both Houses of Congress, and the waiting-period form, i.e., proposals go into effect after laying before the Congress for a specified period unless negated through regular legislation. These three forms of the device should be utilized in terms of the type and vigor of control needed, the waiting-period being best suited for fields which require the least stringent control and the one-House veto being best suited for fields which require the most sensitive type of control. In addition, as the history of the Reorganization Act of 1949 demonstrates, when necessary greater precision can be added to the device through use of the constitutional majority proviso as a means of moderating the harshness of the form of veto control utilized.<sup>67</sup>

<sup>67</sup> The question of whether the veto should be before or after the fact, i.e., whether proposals are to be immediately effective but subject to disallowance for a specified period or not effective until subject to disallowance for a specified period, is not a meaningful one in the U.S.A. Though theoretically before and



*Safeguards for Protection.* There is still another phase to the structural problem. In the construction of the veto as in the construction of a suspension bridge basic material must be molded not only in relation to its designated function but also in relation to the demands of safety. As a result there are basic safeguards which must be included as integral features of the mechanism if the veto is to serve as an effective means for popular government.

There must be provision for cloture and for mandatory discharge from committees. With regard to those matters which go directly to committee instead of to committee only upon the introduction of a disapproval resolution, e.g., deportation suspension orders, the committee should be required to issue a report on those matters it does not propose for disallowance.<sup>68</sup> Such a requirement would serve to weaken the possibility or the effect of practical control by committees. However, in those cases in which the reporting requirement renders a highly necessary instance of shotgun review impractical or impossible, it may be waived. Along with all this, legislation introduced under the waiting-period form should be privileged. Such a strengthening of the waiting-period form would prove very useful. For, in the face of the relative innocuousness of the waiting-period as presently constituted Congress has been forced to rely on other forms of the device even though the intensity of control effected by such means is out of all proportion to the significance of the area.

Similarly, care should be taken to insure that the President has effective control over the process of administrative formulation necessitated by the device. The veto must not become an instrument for strengthening agency-committee relations at the expense of control and direction by the chief executive.

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after the fact forms could also be utilized according to the type and sensitivity of control needed, there is little possibility that Congress would ever utilize after the fact negation. However, in contrast to Great Britain this is no great loss in the United States. After the fact negation by nature is not well-suited for checking areas of most vital policy significance. Aside from its great potentialities for situations of grave crisis, its main use must be with regard to administrative rule-making. But even in those few instances where veto review of administrative rule-making is desirable nothing is sacrificed by reliance on before the fact negation.

<sup>68</sup> Unfortunately, few pieces of veto legislation have contained this requirement. One which did was one of the most successful and beneficial instances of veto review—The Surplus Property Act of 1944 (58 Stat. 775).



The veto must be framed in such a way as to satisfy the maxim of indirect responsibility outlined above. If it is not, the device will wreak havoc with Presidential endeavors to provide coherent and integrated leadership. To illustrate inadequate provision for indirect responsibility consider the valley authority bills of 1947. These bills sought to establish valley authorities in the Missouri, Columbia and Savannah River valleys and contained an arrangement whereby the authorities' comprehensive development plans went into effect unless disapproved by concurrent resolution. But Section 11(a) of S. 1156 and Section 8(a) of S. 1647 merely provided that the Corporation submit its plan simultaneously to Congress and the President within two years after the bill's enactment. Thus, if the bills had passed, the veto procedure would have failed to secure effective participation by the President. For since he did not have the opportunity to revise or veto a plan before it went to Congress, there was no assurance that a plan would be in accord with national policy for resource use or allocation. To avoid such situations each implementation of the veto device ought to guarantee prior Presidential review. Administrators must not be allowed to submit their proposals directly to the Congress; rather, their proposals should be submitted to the Congress through the President. For example, the Lease-Purchase Act of 1954 provides that "no proposed lease-purchase agreement shall be executed . . . unless such agreement has been approved by the Director of the Budget, as evidenced by a written statement . . . that the execution of such agreement is necessary and is in conformity with the policy of the President."<sup>69</sup>

Moreover, the veto in each specific instance must be formulated in such a way as to emphasize broad policy and performance, not detail. Proper drafting is essential if the veto is to be contained within the realm of broad accountability. Perhaps the best illustrations of such drafting are the Atomic Energy Act of 1946, the valley authority bills of 1947 and the Rubber Producing Facilities Disposal Act of 1953. Section 7(b) of the Atomic Energy Act of 1946 provided that no license with respect to non-military utilization of atomic energy could be issued by the A.E.C. until a report submitted by the A.E.C.

<sup>69</sup> H. Rept. 1923, 83rd Cong., 2nd Sess.

with respect to such utilization had lain before Congress for 90 days. This section also provided that such a report had to deal with the social, political, economic and international effects of such a utilization plus the Commission's recommendations for supplemental legislation. In this way the Act directed Congress' attention to issues of broad policy.<sup>70</sup> Section 2 of the Rubber Producing Facilities Disposal Act of 1953 instructed Congress to consider the extent to which a disposal plan fostered "the development within the U. S. of a free competitive synthetic rubber industry."<sup>71</sup> With regard to the valley authority bills, though poorly framed with respect to indirect responsibility, they were drafted in such a way as to insure broad policy accountability. For individual projects were not subject to review; instead, Congressional attention was centered on a sweeping comprehensive plan of regional development. Lastly, laying time before Congress under all forms of the device should be specified to include only days when Congress is in session. Unless this is done, Congressional review is not adequately guaranteed. For example, on March 20, 1933 the Economy Act of that year was amended to provide that executive orders had to lie before Congress for sixty days rather than sixty legislative days. The result was that President Roosevelt submitted his most important changes under the authority of the act on June 10, 1933, six days before Congress adjourned; nonetheless, sixty days later these orders went into effect.

#### CONTRIBUTION OF THE VETO

As indicated above, in both the enactment of law and the execution of law the proper role of the executive is leadership, whereas the proper role of the legislature is criticism and control on behalf of the nation. Assuming that the veto is correctly utilized and structured, these notions serve as a basis for delineating the veto's potential contribution to the success of popular government. But first one point must be recognized. Earlier in this paper we indicated that the administration must be held accountable for policy and performance prenatally and postnatally, that is, for policy proposals in the course of legislation and for policy decisions and administrative performance

<sup>70</sup> 60 Stat. 764 (1946).

<sup>71</sup> 67 Stat. 408 (1953).

in the course of execution. However, the veto functions simultaneously as a check on the enabling act and a check on executive proposals, and in so doing it obscures the distinction between prenatal and postnatal accountability. Nonetheless we should still keep this distinction in mind when we speak of the veto's contribution to Congressional control and executive leadership. For though the veto destroys the formal distinction between prenatal and postnatal accountability, the logical foundations of the distinction remain meaningful. In so far as we point out that the veto augments Congressional control, control should be understood as referring to both the contribution that Congressional criticism makes to bringing the legislative process into closer harmony with the will of the people and the contribution that it makes to holding the executive accountable for responsible and efficient policy decisions (or efficient administrative performance if veto is used in this regard). In so far as we point out that the veto augments executive leadership, leadership should be understood as both leadership of the legislative process through the presentation of balanced policy programs and leadership of the discretionary and operational aspects of administration through direct control and integration. In other words even though the veto combines postnatal and prenatal accountability in one process, its contribution remains two-fold in essence.<sup>72</sup>

*Contribution to Congressional Control.* Basically, in all instances of proper formation and utilization the veto serves as an effective means for subjecting administration to the control of the Congress. It does not impair any of the other instruments of Congressional control; its check is a vigorous one; it centers attention on the more vital aspects of policy and performance; and it furthers majority control over enactment and execution.

<sup>72</sup> Though the veto by nature simultaneously checks administration for both policy decisions and policy proposals, its emphasis may differ in its various applications. That is, the veto may be primarily directed to securing policy proposals for legislative consideration or, on the other hand, it may be primarily directed to checking the substantive nature of executive decision-making. For example, the Reorganization Act of 1939 placed more emphasis on the task of defining policy for legislative consideration than the Alien Registration Act of 1940 which, rather, emphasized the task of checking administrative decision-making. However, again, some exceptions must be indicated. When the veto is used to check administrative performance, it can only play a postnatal role. In addition, the waiting-period form of the veto can be restricted to a purely postnatal role, especially if used to check administrative rule-making.

Nevertheless, the veto's contribution to popular government does not lie merely in the fact that it is in itself an effective instrument for Congressional control. Congress has many potent instruments of control. The significance of the veto lies in its strategic and distinctive advantage as a check on the very effectuation of executive proposals. The primary contribution of the veto is that it extends the sway of effective Congressional criticism and control over areas of administration hitherto feebly supervised. In an earlier section of this paper we delimited a middle-ground area of administrative decision-making in which the present means of Congressional oversight are inadequate. Let us illustrate by specific examples the veto's potential contribution in this area. Perhaps the best illustration of the way the veto can be applied advantageously to fields where clear standards cannot be set is the manner in which the Atomic Energy Act of 1946 dealt with the problem of developing and utilizing atomic energy for non-military purposes. Here the nature and novelty of the subject matter precluded the setting of precise standards and long-range goals in the authorizing legislation. Yet through use of the reporting requirement contained in Section 7(b) of the Act, Congress was able to retain control without denying the administrative agency the flexibility that is so essential in the development and exploration of complex and novel fields.<sup>73</sup> Indeed, the logic of the device becomes all the more evident when the possible alternatives are considered. As James Newman,<sup>74</sup> Special Counsel of the committee which prepared the legislation, has pointed out,

This is doubtless the most effective provision that could have been framed under the circumstances . . . the Commission might have been left free to issue licenses as it saw fit, with only the very general

<sup>73</sup> The Atomic Energy Act of 1954, in response to criticism by private industry (see D. Lilienthal, "Toward an Industrial Atomic Future," *Collier's*, June 15, 1950), does not contain provisions for such a report or for veto review of it. Instead, Section 202 of the act states, "During the first sixty days of each session of the Congress, the Joint Committee shall conduct hearings . . . for the purpose of receiving information concerning the development, growth, and state of the atomic energy industry." However, the act does subject electric utility contracts negotiated by the A.E.C. and international information exchange agreements to waiting-period review by the Joint Committee on Atomic Energy (68 Stat. 919).

<sup>74</sup> James R. Newman, *The Control of Atomic Energy* (New York, 1948), pp. 133-34.

policy statement of the act for guidance. This would have entrusted the Commission with sweeping powers over the whole economy such as no democracy would be willing to entrust to appointive officials . . . [or] Congress might have reserved to itself the exclusive right to decide on licenses. . . . This would have delayed the constructive development of atomic energy by many years. Or, finally, the Commission itself might have been given a monopoly over all operations involving the use of atomic energy. . . . The result of this provision would have been to embark on a steadily expanding program of socialization. . . . Regardless of the substantive merits of such a program . . . an act for the domestic control of atomic energy is not an appropriate instrument for its achievement.<sup>75</sup>

F.E.P.C. offers another good example of the veto's utility as a device for entrusting the task of detailed exploration to competent administrative agencies while retaining sensitive Congressional control over the nature of specific policy decisions and the shaping of general policy. To quote Schauffler once again, "The problem, as suggested by the experience of various State Commissions, is how to bring about a gradual adjustment of social attitudes concerning nationality, race, and religion, attitudes the intensity of which cannot be estimated in advance. Here the application of a legislative veto system is eminently reasonable. The long-term ideal can be set forth in regular legislation; and then the issuance of regulations approaching this ideal in gradual steps (determined by the strength of the resistance encountered) can be kept under Congressional control through a case-by-case clearance requirement."<sup>76</sup>

In addition to fields in which clear standards cannot be defined, the middle-ground area also includes fields which inherently repel the normal means of Congressional control. Note the Rubber Producing Facilities Disposal Act of 1953. Under the terms of the act a temporary commission was set up to dispose of the Government's synthetic rubber plants. How could Congress have insured administrative adherence to

<sup>75</sup> In all fairness the other side of the case should be acknowledged also. With reference to the veto in this act David Lilienthal, after he left the Commission, said, "This is one of the most appalling reversals of our way of doing things. . . . If such a veto of industrial advance had been in the law-books when the locomotive was first developed, the outcry of its competitors, the stagecoach and the canal, might well have barred the progress of our railroads. . . . [The veto] ought to be buried fast and buried deep." (*Collier's*, June 15, 1950). However, even if Lilienthal is right and this was a misapplication of the veto, his case only supports the basic point made in the text—that the veto can serve as a means for effectively controlling areas in which precise standards cannot be defined.

<sup>76</sup> Schauffler, *op. cit.*, pp. 58-59.

the standards contained in the act (a fair return on the sale and a competitive synthetic rubber industry) through its regular means of control? Appropriations—the commission would require the same amount of money no matter how it disposed of the plants. Investigation—this would have come too late to rectify the damage. Legislation after disposal—here there would be vast difficulties due to constitutional provisions protecting the sanctity of property rights. In short, the only possible effective control was one which could be exercised over the disposal plan before it went into effect, i.e., veto review.<sup>77</sup>

However, the veto need not be restricted to those fields where it alone provides adequate Congressional oversight. The device can also be extended to those areas in which it serves as the most effective means of control. It may be desirable to subject certain key areas of policy and performance to veto review even though these areas may be adequately controlled through other devices. Take, for instance, the case of valley authorities. There is little doubt that T.V.A. is adequately controlled through appropriations, investigations, and so on. Still, it may well be that the veto procedure provided for in the valley authority bills of 1947 offers a more efficacious form of oversight. In surveying the comprehensive development plan of a valley authority not only would Congress' attention be centered on basic issues of policy; in addition, Congress would possess a more direct means of holding the authority accountable for policy than it now possesses under the T.V.A. arrangement.<sup>78</sup>

In conclusion, the veto has both a primary and secondary contribution to make to the establishment of adequate administrative accountability. First, it can be used to establish Congressional control where it was formerly non-existent. Second, it can be used as a more effective alternative to other forms of Congressional control.

*Contribution to Executive Leadership.* The veto's potential

<sup>77</sup> The efficacy of this form of control has also been well illustrated by a case study on the disposal of the aluminum plants under the authority of the Surplus Property Act of 1944, as amended in 1945 (59 Stat. 546). See H. Stein (ed.), *Public Administration and Policy Development*, "The Disposal of the Aluminum Plants" (New York, 1952), p. 313.

<sup>78</sup> S. 1647 and S. 1156, 80th Cong., 1st Sess.



contribution to the success of popular government is not limited to the realm of Congressional control. The crowning achievement of the veto is that it can concomitantly provide for both Congressional control and executive leadership. For, happily, the veto's inherent method of approach is not of such a nature as to require the sacrifice of executive leadership on the altar of accountability. Rather, it establishes accountability through the institutionalization of executive leadership. If the veto is properly framed, every instance of its use insures both that legislative attention will be centered on balanced programs submitted by the President and that the discretionary and operational activities of administration will be directed and integrated by the President. Moreover, if properly framed and applied, the veto tends to free executive leadership from many of the destructive and frustrating aspects of Congressional control. The veto generates trust and confidence, thus eliminating many of the petty interferences to which legislators are otherwise prone; it invests Congress with a sense of responsibility, thus serving to reduce the number of irresponsible charges and demands made by legislators; and it induces Congress to press for better administrative coordination since balanced programs are most essential in veto review, thus enervating Congressional desires for atomizing administration.

But, as in the case of Congressional control, the great significance of the veto does not lie merely in the fact that every proper instance of its use institutionalizes executive leadership and frees it from the ruinous features of Congressional control. More important, the veto makes feasible an extension of executive leadership to areas of decision-making which now stand in vital need of the competence and/or the integration that executive leadership furnishes. Before the veto appeared on the scene any such extension of executive leadership was impossible. For though the executive might be a better or even the only qualified body to render decisions in certain fields, Congress was strongly inclined to refuse the executive decision-making power if it thought the executive could not be subjected to effective Congressional control. Of course, at times Congress has delegated power to the executive even though it felt it could not control. The point is that to a significant extent



it has not.<sup>79</sup> In certain important areas of decision-making Congress has felt that it had to obstruct the executive merely in order to maintain its own place in the governmental system.

In large part the veto solves this oversight dilemma. It comes as a palliative for Congressional paranoia since it presents the Congress with a meaningful alternative to outright delegation. As a result executive leadership can now safely be strengthened in three respects. First, with respect to those decisions the legislature is unwilling to make but would not previously delegate outright, what is little appreciated is how frequently the divergent sectional, economic and political interests manifest among the numerous members of a legislative body make agreement a lowest rather than a highest common denominator.<sup>80</sup> Yet if the matters are pressing, and often they are, effective democracy can countenance no stalemate. Executive leadership structured in terms of a veto arrangement offers a facile and efficacious method of settlement. Note the Reorganization Act of 1939.

Second, with respect to those decisions the executive is better qualified to make but which the legislature would not previously delegate outright, executive leadership institutionalized through a veto arrangement can provide for great advances in rational and coherent policy making. The field of resources offers a good illustration.<sup>81</sup> Instead of authorizing individual water

<sup>79</sup> In these instances Congress has tried either to decide the matters itself or has set up independent regulatory commissions. Neither solution is satisfactory. Congress has not the time, expertise, or information to properly reserve these decisions to itself; and its ability to control "quasi-legislative" agencies on these matters is just as limited as its ability to control the executive. Note the comment of the President's Committee on Administrative Management: "[The Commissions are a] . . . headless 'fourth branch' of the Government, a haphazard deposit of irresponsible agencies. . . . The Congress has found no effective way of supervising them. . . ." President's Committee on Administrative Management, *Administrative Management in the Government of the United States* (Washington, 1937), p. 36. Perhaps, then, the only profit Congress derives from employment of commissions is a psychological one, i.e., the hated executive is denied extension of its authority.

<sup>80</sup> John R. Millett and Lindsay Rogers, "Legislative Veto and the Reorganization Act of 1939," *Public Administration Review*, Winter, 1941, p. 177.

<sup>81</sup> The Reorganization Acts of 1939, 1945, and 1949, the Atomic Energy Act of 1946, the Alien Registration Act of 1940, the Federal Airport Act of 1946, et al., also testify to the utility of the veto in this regard. The Airport Act abbreviates the regular appropriations process. Section 8 of this act requires the Civil Aeronautics Administrator to prepare a national airport plan and to submit to Congress annually a request for authority to undertake the projects contained in the plan. In addition, this section provides that, ". . . the Administrator may consider the appropriation of funds by Congress as granting the authority requested

resource projects in biennial omnibus flood control bills or river and harbor bills, Congress could pass a basic law setting out in some detail the standards to be met by any proposed water project desirable of development. The water development agency could be authorized both to undertake any investigation, not having to rely on Congress to authorize each survey, and to recommend for construction any project that met the standards of the basic law. These approval recommendations could then go into effect subject to some form of veto review.<sup>82</sup> In this way decisions with respect to the projects best suited to serve the unified development of a region would be placed in the hands of those best qualified to make them and the disruption of integrated resources policy by special interests would be decreased.<sup>83</sup>

Third, with respect to those decisions the Congress is incompetent to make but would not previously delegate outright, the discussion contained in the first part of this section has adequately illustrated the advantages in terms of expertise that can be gained from an extension of executive leadership through utilization of the veto.

In conclusion, the veto has great potentialities as an instrument for institutionalizing executive leadership, freeing executive leadership from the petty features of Congressional control, and extending the scope of executive leadership. In so doing, the veto's latent contribution must be appreciated not merely in terms of executive leadership *per se*, but, more basically, in terms of the contribution heightened executive leadership makes to the cause of effective democracy.

*Possible Ill Effects.* Though the dangers inherent in improper utilizations of the mechanism have been indicated at various points in the text, let us, for the purposes of clarity, briefly bring them together here. If the veto is expressed through the committee-action form, it can serve as an effective means for extending minority control over vast new areas of policy. Moreover, if the veto is not framed so as to insure indirect

unless a contrary intent shall have been manifested by the Congress by law or by concurrent resolution. . . ." In other words, Congress can still veto particular projects through amending the language of the appropriations bill (60 Stat. 164).

<sup>82</sup> A. A. Maass, "Congress and Water Resources," *American Political Science Review*, September, 1950, p. 30.

<sup>83</sup> Congress still retains control over the priority of projects through the appropriations process.

accountability, it can serve as an efficacious means for isolating the President and establishing closer relations between committees and their "pet" agencies. Lastly, the dangers of misapplication are manifold. The veto can be applied to fields within the area of broad accountability but not suited for the type of inflexible control it establishes; it can be applied to fields suited for its method of control but not contained in the area of broad accountability; and it can be utilized to control fields which are neither within the area of broad accountability nor suited for its method of control. In each of these misapplications the veto hampers the executive for the purposes of overly stringent Congressional control rather than combining the advantages of executive leadership and Congressional control as is the case in its proper applications.

In closing, we cannot foretell with any large measure of accuracy what the future holds for the veto. Whether its ultimate results will be beneficial, pernicious or inconsequential to the cause of American democratic government remains in doubt. Certainly, it has vast potentialities for both great harm and great benefit. Only one thing seems sure. The veto will endure as a permanent feature of the American political scene. Repeated usage since 1939 has endowed the device with a theoretic rationale adequate to insure its survival and has clothed it with sufficient dignity to allow it to press its claims without timidity.<sup>84</sup> These facts when combined with the exigencies of accountability will in certain situations suggest and even demand its utilization. At worst, the variety of forms through which the veto is now expressed might be reduced and the mechanism itself might be used less extensively and less intensively than at present. But the integral features of the mechanism will remain and continue to be utilized. Congress will not and cannot totally ignore the desirability of subjecting certain executive actions to some further form of legislative assent.

<sup>84</sup> Note the change in attitude that took place in Congress between the Reorganization Act of 1939 and the Reorganization Act of 1945. Contrast 84 Cong. Rec. 2943-51 with 91 Cong. Rec. 10713.

*Note:* Developments since the preparation of this article: In the closing months of the 84th Congress the veto occupied the legislative spotlight in a manner unparalleled in its past history. In this short period the veto figured prominently in the passage of five measures, four of which are of wide importance.

The bitterest controversy arose over the Military Construction Act of 1956.

This measure as originally passed (H.R. 9893) subjected military housing contracts and Talos missile sites to committee approval. When President Eisenhower rejected the bill because of its veto features, Congress modified the military housing provision to require only waiting-period review, but it refused to reauthorize Talos missile site construction. Congress' feeling on the matter was that without some stringent form of veto review it would have no adequate or practical means of insuring that Talos missile development did not result in mere wasteful duplication of existing facilities. Of almost equal intensity was the debate over the veto provisions contained in Section 638 of the Defense Appropriation Act of 1956. These provisions were finally deleted from the 1957 Act, but another bill (H.R. 7992) which would have put them back into effect in a one-House instead of the original committee-action form passed the House and was before a Senate committee when the session closed.

On the other hand the drive to liberalize the veto provisions in the Small Watershed Act of 1954 encountered little opposition. The new version of the act does away completely with the section in the original act which required each and every project proposal to undergo waiting-period review. In place of the waiting-period requirement the present act subjects projects involving a federal cost of more than \$250,000 to the same restrictions which formerly applied only to projects embodying a structure of more than 2500 ac. ft. total capacity. Thus no money can be appropriated for projects falling into either category unless such projects are approved by the appropriate substantive committees of the House and Senate. Also liberalized in the closing days of the session was the requirement for waiting-period review of National Park concession contracts and leases. The new provision (P.L. 712) requires waiting-period review only for those contracts and leases which involve a gross annual business of over \$100,000 or which involve a period of more than five years duration. Such liberalizations indicate that at least procedurally overly restrictive uses of the veto may prove to be self-defeating.

Yet none of these measures, important as they may be, bears as much significance for the future course of veto development as the action taken in the Small Projects Act of 1956. This act permits either of the appropriate House and Senate committees to disallow loans or grants proposed by the Secretary of the Interior for purposes of aiding state and local agencies in the construction of small irrigation projects. However, in an unprecedented move, the act also gives Congress the power to override any veto action that its committees might take in striking down such grants or loans. This arrangement was not considered in the main body of the article, but it does seem to suggest a promising method for containing the committees in their proper roles as servants of the Congress in those areas where veto control must involve the review of large amounts of material.

### PART III

## MONETARY AND FISCAL PROBLEMS



TAXES AND TREASURY DISBURSEMENTS,\*  
REGIONAL AND STATE DIFFERENCES,  
1934-1954, 1939, 1952, 1953, 1954

*Seymour E. Harris*<sup>1</sup>

THE following is a copy of the covering letter which accompanied the report when it was sent to the Honorable Herbert H. Lehman, U. S. Senate.

December 7, 1955

The Honorable Herbert H. Lehman  
U. S. Senate  
Washington, D. C.

Dear Senator Lehman:      In Re Federal Tax Burden and  
Federal Disbursements:  
By Regions and States, 1934-1954

I enclose the material on the distribution of taxes and Federal disbursements by regions and states. You will recall that at the hearings on flood insurance before the Sub-Committee of the Senate Banking and Currency Committee under your chairmanship (Boston, November 9, 1955), I presented some material on the extent to which the South and the West were subsidized by the Northeast and a few of the Middle Western states. The point of emphasis was that, in view of these large and continued transfers, a strong case could be made out for a generous program of flood control, flood aid, and flood in-

\* Reprinted from Report to the Conference of New England Governors "New England Textiles and the New England Economy," Seymour E. Harris, Chairman of New England Governors' Textile Committee, February 1956.

<sup>1</sup> I am indebted to the New England governors for providing the funds which made this study possible; to Mr. Peter Kenen, a graduate student at Harvard University (and his assistant, Miss Florence Wallach), who supervised the statistical work and needled at least 25 agencies in Washington for information; to Mrs. Joan Eckstein for much research help; to the wonderful contributions of the Harvard Computational Laboratory and, in particular, to Mr. J. E. Van Tassel, Jr., its manager; to Mrs. Anna Thorpe for the typing; and to the members of the New England Governors' Textile Committee, who have given me much independence in carrying on and much useful advice at all times. The Byrd Committee's work has also been very helpful, and I should give special thanks to a number of economists who have allocated taxes on an incidence basis, but especially to Miss Mabel Newcomer and to Miss Selma Mushkin (assisted by Miss Crowther), of the Public Health Service, who is the latest of this group of pioneers.



surance which might send back a small part of the money transferred and being transferred via the Treasury from the Northeast.

You urged me at that time to send this material for the use of the Senate Hearings. Since then you have assured me that the hearings would be kept open until December 23. I was doubtful that I could finish this study in time; but the miracle of electronics has helped and the material is now available. Your Committee is getting the first release of this material.

I should like to emphasize the point that this study has been made possible by the generous help of the New England Governors, who have financed the New England Governors' Textile Committee. That Committee, in turn, has used some of its funds to hire research workers, pay for the use of IBM machines and for the typing required for this study.

The New England Governors for years have been concerned with the problem of the decline of textiles, the migration to the South, and similar problems. The Middle Atlantic and some of the North Central industrial states should be equally interested. The losses of textiles by New York, New Jersey, and Pennsylvania have been as great as those of New England. Although with a larger economy the Middle Atlantic states have not felt the losses as much.

In New England we are all aware that the South has great possibilities as an industrial area—among her advantages are her determination to get ahead, proximity to rich natural resources, large reservoirs of agricultural labor being squeezed off the farm, and proximity to rich markets. But we have also been aware that part of the gains are to be associated with the great political influence of the South. Much of the aid from the Federal Government is to be approved and raises no serious questions. But in such matters as labor legislation, mergers, tax privileges, use of Federal credit, and tax exemptions some questions may be raised.

We have insisted for years that any one Federal policy should be considered in the light of all Federal policies. It is not fair to consider tariff (say) or agricultural policies, without a consideration of what all Federal policies do to an industry or region. Hence the importance of an over-all view of regional effects of taxes and Federal disbursements.

## TAXES AND TREASURY DISBURSEMENTS 179

The present study is an attempt to highlight one important aspect of this problem: to what extent does the Federal Government serve as a mechanism for transferring cash from rich to poor, from North to South and West, and under what programs? An examination of the figures for 140 programs over a period of 20 years and with minute studies for 1939, 1952, 1953, and 1954 will give Congressmen an opportunity to make decisions on each program with an awareness of the over-all problem of transfers of cash.

### THE MAIN OUTLINES OF THE STUDY

(All numbered references are to paragraphs in the text.)

#### *Taxes Borne, 1934-1954*

1-3. The first table presents the percentage of taxes borne by states over a 20-year period broken down by sub-periods. It is clear that the rich states bear taxes in greater proportion than their proportionate income. But as the poorer states grow, their share tends to rise.

#### *Federal Disbursements in Relation to Taxes Borne*

4. Disbursements under 140 programs (grants and aids) reveal variations of as much as \$38.62 of Federal disbursements per \$1,000 of taxes borne by Delaware to \$534.46 for Mississippi. Ten poor states receive 10 times as much as 10 rich states in relation to taxes borne.

5. Sparsely populated Western states and Southern states gain especially from these transfers. Four Middle Atlantic, three New England, two Middle Western, and one Far Western states are the most generous contributors.

#### *Same Comparison: New England and the Competitive South and Rich and Poor States*

6-7. Over a period of 20 years, New England gets back but 31 per cent of the amount of taxes borne relative to what 5 major Southern industrial states get back; the corresponding rate for the 10 richest *vis-à-vis* the 10 poorest states is 19 per cent.

*Expenditures, Loans Closed and Insured, 1939*

8-10. For 1939, a comparison of 4 Northern states (New York, Illinois, Massachusetts, Connecticut) and 5 Southern states (Alabama, Georgia, North Carolina, South Carolina, and Tennessee) reveals that the Southern states received  $2\frac{1}{2}$  times as much Federal disbursements relative to income as the 4 Northern states. *Vis-à-vis* New York and Connecticut, the ratio was 3 to 1. (Note only 60 per cent of expenditures are covered.)

11-12. Again, for 1939, New England with 8.2 per cent of the nation's income received but 6.1 per cent of the Federal expenditures and 3.3 per cent of the loans closed. The 10 richest states profited from Federal expenditures equal to two-thirds their percentage of income; but the 10 poorest states, with 9.6 per cent of the nation's income, accounted for 17.8 per cent of the expenditures.

*Same Comparison: 10 Northern and 10 Southern and Western States*

13-14. In 1939, 10 Southern and Western states profited from Federal disbursements almost  $5\frac{1}{2}$  times as large relative to tax burden as 10 Northern states; in loans closed, the 10 Southern and Western states received 10 times as much relative to taxes borne as the Northern states. (Massachusetts, Connecticut, Rhode Island, and New York are among these states.) *It is clear that the expansion of the South and West is beset with smaller obstacles than that of the older states has been.*

*1939: Taxes Borne and Federal Disbursements, Regional and Rich and Poor*

15-16. In relation to 5 major Southern industrial states, New England received back in expenditures one-third as much relative to taxes borne; and Rhode Island, Connecticut, and Massachusetts, 30, 21, and 37 per cent, respectively. The 10 richest states received back much less than New England in relation to taxes borne in Federal outlays and loans.

*A Study of Taxes and Expenditures for 1952*

17-18. A study for 1952 considers not only Federal grants and aids to individuals but also market transactions—e.g., govern-

## TAXES AND TREASURY DISBURSEMENTS 181

ment purchases. It is clear that some states gain more than others according to the nature of the government outlays.

### *Revenue Incidence and Federal Expenditures*

19-24. The 1952 expenditures are analyzed on the basis of benefits received or the incidence of the disbursements. Necessarily the results can be held to be only roughly tenable. New England, the Middle East, and New York reveal receipts from Federal disbursements (average of benefits and disbursements) equal to about 75 per cent of taxes borne. Of course, the South and the sparsely populated Northwest gain greatly.

### *Tax Burdens*

25-26. Tax burdens vary much more than Federal receipts—a minimum of tax burdens per capita was \$112 in Mississippi to \$1,015 in Delaware. On an incidence basis, since sales to government are included, the rich states lose less than on a benefit criterion—but even on this basis, the Southeast comes off almost twice as well as New England on a tax-revenue basis. Twenty-nine states with incomes below average received 75 per cent more in revenues contributed than the poor states. Connecticut and Massachusetts paid out \$1,103 million in excess of what they got back; Rhode Island, \$123 million; and 3 other New England states, \$47 million.

### *Distribution of Federal Payments by Types*

27. Federal income payments (exclusive of purchases of goods and services) greatly benefit the South *vis-à-vis* the North.

28-31. On government contracts, New England's record is much better than on all Federal disbursements. Here, of course, is a competitive field. From July 1950-March 1954, New England received \$8.1 billion of \$101 billion of military procurement and construction awards—a level below its percentage of manufacturing employment but in excess of its percentage of income. Connecticut received 3 times as much as Massachusetts, however, when the figures are related to the income of both states. New York's proportion was 15.5 per cent. (Her income averaged a little over 12 per cent for 1950-54.) Once adjustments are made for place of production rather than for

place where the contract is consummated, New England's share is reduced from 8.0 to 7.5 per cent and New York's, from 15.5 to 10.1 per cent.

*Federal Tax Burdens, Federal Disbursements and National Income, 1954*

32. *A master table for 1954 gives Federal disbursements, Federal taxes borne, and the relation of these and of disbursements.* The original table covered 140 disbursement programs; but with those accounting for less than \$10 million omitted (they add up to less than \$1 billion), the table treats only 75 programs.

33-34. In only 18 out of 75 programs does New England receive back percentagewise as much as she puts into the Federal program. In the grant and aid programs, her receipts are equal to but 81 per cent of the amount suggested by her relative income.

35-40. In the category 2A, grants, etc. to individuals and groups, New England received more than indicated by her share of income. But the explanation here is that this category is primarily an insurance one. New England does not fare well in the category of loans or of projects within states. (In the last, the major item is civil projects of the Army Corps of Engineers—New England profited from but 0.62 per cent of the national outlays, a figure less than 1/10th of her relative income.)

41-42. New England profited little from Federal loan programs; they were used primarily to bolster or stimulate other parts of the economy. New England's loans were but 1.26 per cent of the nation's \$6.2 billion. But in guarantees her record was much better.

43. Of salaries disbursed by the Federal Government, New England received 88 per cent of the amount indicated by her income; but less, of course, in relation to taxes.

44-45. For all expenditures considered (\$17.8 billion) New England received an amount equal to 96 per cent suggested by her income and much less relative to taxes borne—but the figure is inflated, of course, by the large amount of insurance payments. Her receipts from loans were but one-fifth that indicated by relative income.

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### *Disbursements in Relation to Taxes Borne, 1954*

46-50. As might be expected, New England's receipts of Federal payments are much lower relative to taxes borne than to income. Of 75 substantial programs, New England receives amounts per \$1,000 taxes borne in excess of the national total only in 6 programs.

51. On this criterion, New England received 82 per cent of what might be expected from her taxes borne, 16 per cent for loans closed, and 77 per cent for loans insured. For the important assistance and grants, New England's figure was but 69 per cent.

### *Ibid.: New England, New York, The Nation, and The South*

52. On the same comparisons, New England receipts are less than those of the South Atlantic states in 69 of the 75 programs. (In 46 programs, New England's relative share is 50 per cent or more less than that of the South Atlantic states.)

53. The major comparisons are presented in a condensed table in this section. In re the United States, Federal disbursement in New England relative to taxes borne are 82 per cent; New York's, only 63 per cent; disbursements in New England relative to competitive states in the South, 68 and 37 per cent (South Atlantic and East South Central states). For loans, the New England position is much weaker.

54. When insurance payments are eliminated, the contrast of Northeast and South is greatly increased.

### *The Position of New York, 1954*

55-56. New York's net transfers are even larger than New England's, in part because of her higher income and in part (related) her higher taxes. For grants to states and local units, for example, New York's figure is 44 against 69 for New England.

### *Ten Richest and Ten Poorest States, 1954*

57-59. In 1954, the 10 richest states received much more Federal funds than the 10 poorest states. But when allowance is made for relative incomes, the 10 richest states received but 58 per cent as much of Federal expenditures as the 10 poorest and on the basis of taxes borne, only 42 per cent. Of 75 pro-

grams, in only 3 did the rich states get back a proportion in excess of the ratio of taxes borne.

*A Comparison of 1954 and 1953*

60. Finally, we compare the results in 1954 with 1953. Though there are numerous differences in individual programs, the totals are not far apart.

*Then follows the important Master Table, which gives the details by regions and states of disbursements and relation of disbursements to income and taxes borne for 75 programs, each involving more than \$10 million, costing close to \$30 billion in all. The major omission is government purchases in the open market; but these are covered in the 1952 survey. Here we have a breakdown which highlights the shares of government grants, grant outlays within a state, government loans, and government insurance.*

With kind regards, I am

Very sincerely yours,  
Seymour E. Harris

Enclosure

TAXES BORNE, 1934 TO 1954

1. In this study we estimate the relation of Federal taxes borne (i.e., taxes paid corrected for passing on of the burden to others) and Federal expenditures. We have depended upon the Sundelson-Mushkin and the Mushkin-Crowther studies of incidence for 1939 and 1952, respectively.<sup>2</sup> On various assumptions of incidence (e.g., who pays the corporation income tax), they obtain results which allocate the burden of taxes. For our 1934-1954 study we depend in varying degrees upon these two studies for a determination of the taxes borne by these states in the five periods covered in the following table. The 1934-1951 figures of expenditures are derived from the Byrd study,<sup>3</sup> and the 1952-54 totals are obtained from the *Annual Report of the Secretary of the Treasury on the State of the Finances* for the fiscal years 1952, 1953, and 1954.

<sup>2</sup> Sundelson and Mushkin, *The Measurement of State and Local Tax Effort*, Federal Security Agency, 1944, and Mushkin and Crowther, *Federal Taxes and the Measurement of State Tax Capacity*, Public Health Service, 1954.

<sup>3</sup> Senate Doc. No. 101, *Reduction of Non-essential Federal Expenditures: Additional Report of the Joint Committee on Reduction of Non-essential Federal Expenditures*, Congress of the United States pursuant to Section 601 of the Revenue Act of 1941 on Federal Grants-in-Aid to States, 1952.



# TAXES AND TREASURY DISBURSEMENTS 185

## Tax Incidence

Percentage of U. S. Taxes Borne by Each State,  
Fiscal 1934-1954

State	1934- 1939	1940- 1942	1943- 1945	1946- 1948	1949- 1954
Alabama	.730	.773	.793	.813	.855
Arizona	.269	.308	.327	.348	.385
Arkansas	.458	.460	.461	.464	.465
California	7.445	7.963	8.223	8.477	9.002
Colorado	.765	.811	.834	.858	.903
Connecticut	2.231	2.193	2.175	2.156	2.119
Delaware	.723	.649	.613	.577	.502
D. C.	.940	.938	.935	.934	.930
Florida	1.484	1.562	1.601	1.640	1.717
Georgia	1.058	1.116	1.145	1.175	1.232
Idaho	.225	.239	.245	.254	.266
Illinois	7.451	7.492	7.514	7.529	7.577
Indiana	1.852	1.969	2.027	2.086	2.203
Iowa	1.232	1.301	1.335	1.370	1.438
Kansas	.760	.831	.866	.902	.972
Kentucky	.981	1.004	1.014	1.027	1.048
Louisiana	1.014	1.042	1.055	1.071	1.097
Maine	.609	.582	.568	.556	.527
Maryland	1.815	1.815	1.816	1.817	1.817
Massachusetts	4.475	4.287	4.193	4.098	3.912
Michigan	4.112	4.264	4.341	4.414	4.569
Minnesota	1.895	1.852	1.831	1.809	1.766
Mississippi	.390	.395	.398	.402	.406
Missouri	2.449	2.454	2.456	2.458	2.463
Montana	.361	.359	.359	.359	.356
Nebraska	.659	.694	.711	.730	.763
Nevada	.157	.158	.159	.162	.161
New Hampshire	.368	.356	.351	.346	.333
New Jersey	4.290	4.137	4.061	3.983	3.833
New Mexico	.187	.224	.243	.263	.298
New York	19.466	8.227	17.611	16.978	15.755
North Carolina	1.210	1.252	1.271	1.293	1.333
North Dakota	.233	.239	.241	.246	.250
Ohio	5.559	5.626	5.660	5.690	5.761
Oklahoma	.945	.941	.939	.937	.932
Oregon	.677	.805	.869	.934	1.061
Pennsylvania	8.591	8.217	8.030	7.838	7.470
Rhode Island	.763	.722	.801	.682	.639
South Carolina	.477	.525	.549	.574	.621
South Dakota	.230	.243	.249	.256	.267
Tennessee	.941	1.009	1.043	1.079	1.146
Texas	3.574	3.790	3.899	4.005	4.223
Utah	.251	.271	.281	.292	.310
Vermont	.217	.216	.215	.214	.213
Virginia	1.277	1.355	1.394	1.434	1.511
Washington	1.193	1.317	1.379	1.441	1.564
West Virginia	.758	.770	.775	.783	.793
Wisconsin	2.101	2.089	2.083	2.078	2.066
Wyoming	.152	.158	.161	.166	.170
Total U. S.	100.000	100.000	100.000	100.000	100.000

Sources: See text.

2. This table shows the tax burden of each state over five periods in the last twenty-five years. It will be noted that the rapidly growing states (e.g., California, Washington, Michigan, and most Southern states) now account for a larger part of the tax burden than in the early years; and that the slower growing states (e.g., those in New England, New York), a smaller part.

3. It is well to point out here that the New England states (notably Massachusetts) and the Middle Eastern states (notably New York) bear taxes substantially exceeding the proportion of income of these states.

FEDERAL DISBURSEMENTS (AID PROGRAMS) IN RELATION TO  
TAXES BORNE, 1934 TO 1954 (STATES WITH LOWEST  
AND HIGHEST RELATIVE DISBURSEMENTS)

4. The next table gives disbursements under some 140 programs of Federal aid to the states and aid payments to individuals within the states. Here it will be noted that these Federal expenditures for the nation over the years 1934-54 equalled \$118.47 per \$1,000 Federal taxes. In general, the Federal expenditures were low in the richer states *vis-à-vis* the poorer states. The minimum of expenditures per \$1,000 taxes borne was for Delaware (\$36.62) and the maximum (\$534.46) for Mississippi, or 15 times as great. For 10 rich states (largely industrial) the average was \$69.46 per \$1,000 Federal disbursements, or 60 per cent of the national average. For 10 poor states

Federal Disbursements, Aid Programs, per \$1,000 Taxes,  
1934-1954—Ten Rich and Ten Poor States

1. Delaware	\$ 36.62	1. Mississippi	\$ 534.46
2. Connecticut	49.93	2. North Dakota	441.89
3. New York	54.62	3. Arkansas	438.15
4. New Jersey	61.75	4. South Dakota	402.10
5. Maryland	67.98	5. Idaho	331.02
6. Rhode Island	79.83	6. Wyoming	330.73
7. Illinois	81.04	7. Alabama	312.91
8. Massachusetts	85.60	8. New Mexico	309.59
9. California	88.63	9. South Carolina	302.55
10. Michigan	88.73	10. Oklahoma	301.92
	\$694.63		\$3,705.32
Average, 10 states	\$ 69.46		\$ 370.53

# TAXES AND TREASURY DISBURSEMENTS 187

## The Incidence of Selected Federal Programs, Fiscal 1934-1954

State	Aggregate Federal Expenditures (\$1,000)	Aggregate Federal Tax Incidence (\$1,000)	Federal Expendi- tures per \$1,000 of Taxes (\$1)
Alabama	1,541,921	4,927,695	312.91
Arizona	472,735	2,140,098	220.89
Arkansas	1,210,598	2,762,951	438.15
California	4,568,341	51,543,822	88.63
Colorado	1,076,901	5,196,904	207.22
Connecticut	638,176	12,780,207	49.93
Delaware	120,556	3,292,328	36.62
D. C.	609,558	5,557,565	109.68
Florida	1,211,371	9,920,572	122.11
Georgia	1,658,257	7,109,201	233.40
Idaho	506,968	1,531,543	331.02
Illinois	3,645,627	44,982,819	81.04
Indiana	1,564,010	12,655,886	123.58
Iowa	1,402,591	8,293,495	169.12
Kansas	1,163,011	5,507,961	211.15
Kentucky	1,215,800	6,156,988	197.47
Louisiana	1,662,981	6,427,740	258.72
Maine	372,763	3,253,719	114.57
Maryland	736,173	10,827,515	67.98
Massachusetts	2,060,689	24,073,567	85.60
Michigan	2,361,317	26,612,428	88.73
Minnesota	1,618,784	10,700,317	151.28
Mississippi	1,282,530	2,399,692	534.46
Missouri	2,245,810	14,660,675	153.19
Montana	616,186	2,130,551	289.21
Nebraska	956,822	4,409,237	217.00
Nevada	175,229	956,814	183.14
New Hampshire	227,824	2,033,983	112.01
New Jersey	1,448,536	23,458,766	61.75
New Mexico	504,366	1,629,156	309.59
New York	5,401,391	98,895,477	54.62
North Carolina	1,554,671	7,779,740	199.84
North Dakota	648,955	1,468,577	441.89
Ohio	3,159,733	34,061,456	92.77
Oklahoma	1,682,916	5,574,017	301.92
Oregon	870,857	5,806,538	149.98
Pennsylvania	4,167,438	46,028,399	90.54
Rhode Island	317,562	3,977,951	79.83
South Carolina	1,061,367	3,508,040	302.55
South Dakota	620,717	1,543,678	402.10
Tennessee	1,513,329	6,554,544	230.88
Texas	3,945,140	24,292,197	162.40
Utah	512,018	1,770,569	289.18
Vermont	189,362	1,276,937	148.29
Virginia	1,059,211	8,691,092	121.87
Washington	1,374,508	8,822,283	155.80
West Virginia	781,546	4,680,645	166.97
Wisconsin	1,480,281	12,360,700	119.76
Wyoming	327,833	991,255	330.73
Total U. S.*	70,788,050	596,016,000	118.77

Sources: See text.

\* Detail will not add to total as territories and possessions of the United States have been omitted from the detail but are included in the total.

(equally divided between Southern and Western states) the average was \$370.52, or 5+ times as great as that for the 10 Northern states, inclusive of California, and 3 times the national average.

5. Ten states with the largest Federal disbursements *vis-à-vis* taxes borne accounted, then, for almost 5½ times as much relatively as the 10 states which profited least from Federal outlays *vis-à-vis* taxes borne. Among those especially profiting were 5 Southern states and 5 sparsely populated Western states which gain heavily from Federal road disbursements. Among the 10 states experiencing the largest net transfers to the Treasury were 4 Middle Atlantic states, 3 New England states, 2 Middle Western states, and 1 state from the Far West.

#### SAME COMPARISON: NEW ENGLAND AND THE COMPETITIVE SOUTH

6. In another compilation, we compare Federal expenditures (as defined above) and aggregate Federal tax incidence for the New England, South Atlantic, and East South Central states. Federal payments per \$1,000 of taxes collected amounted to \$118.77 for the country, \$80.31 for New England, \$146.64 for the South Atlantic states, and \$277.14 for the East South Central. Significant for North-South competition are the ratios of 55 and 29 per cent of New England *vis-à-vis* the South Atlantic and East South Central states. The large relative gains of the industrial South *vis-à-vis* New England are underestimated here, since the South Atlantic states include Delaware and Maryland. In fact, the figure for New England (\$80.31) is but 31 per cent of that for 5 major Southern industrial competitors of the North (North Carolina, South Carolina, Alabama, Georgia, and Tennessee). *In other words, New England gets back from 140 Federal aid programs over a period of 25 years less than one third as much as was paid in vis-à-vis the receipts and payments of 5 major industrial rivals.*

#### SAME COMPARISON: 10 RICHEST AND 10 POOREST STATES

7. Finally, the 10 richest states (on the basis of 1953 income) received back *vis-à-vis* taxes borne only 19 per cent as much as the 10 poorest states.

## TAXES AND TREASURY DISBURSEMENTS 189

### EXPENDITURES, LOANS CLOSED, AND LOANS INSURED, FISCAL YEAR 1939

8. The material for this part of our study is drawn from the Office of Government Reports, *Activities of Selected Federal Agencies*, 1933-1939. (These cover 60 per cent of outlays.) The year 1939 is studied because it was the last year when military outlays remained relatively small.

#### Fiscal Year, 1939

State	% Income	% Federal Expenditures	% Federal Loans Closed
New York	15.3	8.2	5.4
Illinois	7.7	6.0	7.5
Massachusetts	4.3	3.5	1.6
Connecticut	1.9	1.0	0.6
4 Northern states	29.2	18.7	15.1
Alabama	1.0	1.9	2.6
Georgia	1.3	2.0	3.1
North Carolina	1.5	1.7	1.6
South Carolina	0.7	1.5	1.3
Tennessee	1.2	1.6	2.8
5 Southern industrial states	5.7	8.7	11.4

9. The table for the Fiscal Year, 1939, gives Federal expenditures, loans closed, and loans insured. Again, we should note that the rich Northern states tend to account for a relatively small part of the Federal expenditures, loans closed, and loans insured. In this table I compare relative incomes with relative amounts of the three variables listed here for 4 major Northern states and 5 major Southern industrial states.

"The *direct* Federal expenditures included are certain items for the Department of the Interior, Bureau of Reclamation, War Department and Veterans Administration. These data represent 58 per cent of total Federal expenditures, excluding debt retirement. . . ."<sup>4</sup>

<sup>4</sup> Bureau of the Budget Staff Memorandum, November 10, 1955, *Tabulation of Federal Expenditures, Receipts* . . . , p. 3.

The Incidence of Selected Federal Programs, Fiscal 1934-1954  
New England, South Atlantic and East-South-Central States

State	Aggregate Federal Expenditures (\$1,000)	Aggregate Federal Tax Incidence (\$1,000)	Federal Payments Per \$1,000 of Taxes Collected (\$1)
U. S. Total	70,788,050	596,016,000	118.77
New England	3,806,376	47,396,364	80.31
Connecticut	638,176	12,780,207	49.93
Maine	372,763	3,253,719	114.57
Massachusetts	2,060,689	24,073,567	85.60
New Hampshire	227,824	2,033,983	112.01
Rhode Island	317,562	3,977,951	79.83
Vermont	189,362	1,276,937	148.29
South Atlantic	8,184,052	55,809,033	146.64
Delaware	120,556	3,292,328	36.62
Florida	1,211,371	9,920,472	122.11
Georgia	1,659,257	7,109,201	233.40
Maryland	736,073	10,827,515	67.98
North Carolina	1,554,671	7,779,740	199.84
South Carolina	1,061,367	3,508,040	302.55
Virginia	1,059,211	8,691,092	121.87
West Virginia	781,546	4,680,645	166.97
East South Central	5,553,580	20,038,919	277.14
Alabama	1,541,921	4,927,695	312.91
Kentucky	1,215,800	6,156,988	197.47
Mississippi	1,282,530	2,399,692	534.46
Tennessee	1,513,329	6,554,544	230.88
10 Richest	19,750,615	272,784,034	72.40
10 Poorest	13,206,820	49,255,747	372.96

Sources: See previous table.

10. Whereas the percentage of Federal expenditures to percentage income in fiscal year 1939 was 64 per cent for the 4 Northern states, the percentage was 153 per cent, or almost  $2\frac{1}{2}$  times as great, for the Southern states. A similar comparison for Federal loans closed yields even more favorable results for the South—in fact, the Southern ratio is almost 4 times as great as the Northern ratio for Federal loans closed relative to the proportion of incomes. For New York and Connecticut, with percentages of expenditures to percentage of income 54 and 53 per cent, the percentage of Federal expenditures in these states relative to incomes was only one third as much as that of the 5 Southern industrial states.

# TAXES AND TREASURY DISBURSEMENTS 191

## Selected Federal Expenditures, Loans Closed, and Loans Insured, Fiscal 1939 (\$1,000)

State	Expenditures <sup>a</sup>	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
Alabama	102,067	37,179	7,308
Arizona	39,844	9,053	4,707
Arkansas	94,116	54,606	3,590
California	305,235	96,059	167,294
Colorado	77,133	15,570	7,665
Connecticut	53,738	5,680	9,408
Delaware	9,716	471	1,627
D. C.	81,900	4,294	3,884
Florida	67,218	19,825	22,376
Georgia	105,386	44,714	12,847
Idaho	36,636	20,079	3,015
Illinois	322,951	108,082	58,928
Indiana	138,823	26,722	27,014
Iowa	98,318	98,315	7,935
Kansas	82,026	22,911	9,051
Kentucky	94,644	17,456	8,828
Louisiana	99,740	32,727	9,688
Maine	25,595	4,210	1,998
Maryland	49,558	9,590	13,751
Massachusetts	187,532	22,948	11,297
Michigan	210,430	28,424	77,573
Minnesota	127,340	36,134	12,451
Mississippi	98,794	58,509	5,647
Missouri	164,941	31,645	19,925
Montana	60,864	28,267	2,050
Nebraska	71,440	40,306	5,554
Nevada	13,026	3,440	1,596
New Hampshire	18,018	5,026	1,574

Sources for table: see text on p. 189.

<sup>a</sup> Includes expenditures for the Agricultural Adjustment Administration, the Farm Security Administration, the Soil Conservation Service, the Land Utilization Program, Agricultural Experiment Stations, Agricultural Extension Work, Colleges for Agricultural and Mechanical Arts, Forest Funds, Forest Roads, the Public Roads Administration, the Civil Conservation Corps, Indian Service Work, the Bureau of Reclamation, the Public Buildings Administration, the Public Works Administration, the Works Projects Administration, the National Youth Administration, the Social Security Act, Rivers, Harbors and Flood Control Programs, Mineral Lease Act Payments, Vocational Education and Rehabilitation, the U. S. Employment Service, State Marine Schools, Federal Water Power Act Payments, State Homes for Disabled Soldiers and Sailors, the National Guard, the Veterans' Administration, and the value of surplus agricultural commodities distributed.

<sup>b</sup> Includes loans closed by the Reconstruction Finance Corporation, the Farm Credit Administration, the Commodity Credit Corporation, the Farm Security Administration, the Farm Tenant Purchase Program, the Rural Electrification Administration, the Public Works Administration, the Disaster Loan Corporation, the Federal Reserve Board, the Home Owners' Loan Corporation, and the United States Housing Authority.

<sup>c</sup> Includes loans insured by the Federal Housing Administration under Title I and Title II.



Selected Federal Expenditures, Loans Closed, and Loans  
Insured, Fiscal 1939 (*Continued*)  
(\$1,000)

State	Expenditures <sup>a</sup>	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
New Jersey	136,616	31,082	42,511
New Mexico	38,815	9,564	2,315
New York	440,012	77,319	88,546
North Carolina	92,125	23,296	7,166
North Dakota	48,619	11,985	836
Ohio	324,974	32,709	46,307
Oklahoma	114,812	29,757	13,037
Oregon	58,822	21,989	7,635
Pennsylvania	346,612	35,636	46,046
Rhode Island	26,527	3,066	3,951
South Carolina	78,585	19,222	4,938
South Dakota	49,987	14,744	1,629
Tennessee	87,067	40,050	11,752
Texas	253,304	121,874	47,570
Utah	32,883	7,319	5,093
Vermont	15,961	4,818	1,240
Virginia	71,504	10,130	14,916
Washington	125,114	24,058	20,795
West Virginia	61,375	5,614	6,584
Wisconsin	127,706	21,892	11,480
Wyoming	26,713	8,230	3,159
Total U. S. <sup>d</sup>	5,395,161	1,436,596	906,089

<sup>d</sup> Aside from rounding error, the detail should add to this total; it is for the continental U. S., excluding U. S. Territories.

11. In the next table, we compare the totals for the United States, New England, the Southern states, and the East South Central states. The same general results are revealed. Thus, New England with 8.2 per cent of the nation's income received but 6.1 per cent of the Federal expenditures; 3.3 per cent of the loans closed; and 3.2 per cent of the loans insured. But compare, for example, the East South Central states: they accounted for 4 per cent of income, 7.1 per cent of expenditures, 10.0 per cent of loans closed, but only 3.7 per cent of loans insured. (The small number of large cities in this region explains in part the low percentage for the last.)

12. Finally, note that the 10 richest states with 43.5 per cent of the income accounted for 28.6 per cent of Federal

## TAXES AND TREASURY DISBURSEMENTS 193

expenditures; the 10 poorest states, with 9.6 per cent of the income, accounted for 17.8 per cent of the expenditures. These rich states are largely the industrial states of the Northeast and North Central; and they accounted for Federal receipts equal to one third relative to income (and even less relative to taxes) as compared with the 10 poorest states.

### Selected Federal Expenditures, Loans Closed, and Loans Insured, Fiscal 1939—New England, South Atlantic and East-South Central States\* (\$1,000)

State	Expenditures*	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
U. S. Total <sup>d</sup>	5,395,161	1,436,596	906,089
New England	327,371	45,748	29,468
Connecticut	53,738	5,680	9,408
Maine	25,595	4,210	1,998
Massachusetts	187,532	22,948	11,297
New Hampshire	18,018	5,026	1,574
Rhode Island	26,527	3,066	3,951
Vermont	15,961	4,818	1,240
South Atlantic	483,192	132,862	84,205
Delaware	9,716	471	1,627
Florida	67,218	19,825	22,376
Georgia	105,386	44,714	12,847
Maryland	49,558	9,590	13,751
North Carolina	92,125	23,296	7,166
South Carolina	78,585	19,222	4,938
Virginia	71,504	10,130	14,916
West Virginia	61,375	5,614	6,584
East South Central	382,572	153,194	33,535
Alabama	102,067	37,179	7,308
Kentucky	94,644	17,456	8,828
Mississippi	98,794	58,509	5,647
Tennessee	87,067	40,050	11,752
10 Richest	1,544,911	357,737	398,909
10 Poorest	916,215	336,774	75,949

Sources: See text.

\* For relevant notes, see last table.

1939: FEDERAL EXPENDITURES, LOANS CLOSED, AND  
LOANS INSURED—10 NORTHERN AND 10 SOUTHERN  
AND WESTERN STATES

13. In two final tables in this section, we compare tax burdens and Federal expenditures, loans closed, and loans insured. Again, the rich Northern states experience "losses" relative to Southern and Western competitors. Thus, here we compare 10 Northern and 10 Southern and Western States.

Value Per \$1,000 of Taxes Paid of Northern States

	Federal Expenditures	Loans Closed	Loans Insured
Delaware	\$243	\$ 12	\$ 41
Connecticut	437	46	76
New York	410	72	82
New Jersey	577	131	180
Maryland	495	96	137
Rhode Island	630	73	94
Illinois	786	263	143
Massachusetts	760	93	46
California	743	234	407
Michigan	928	125	342
Average, 10 Northern states	600.9	114.5	154.8
U. S.	978	260	164

Value Per \$1,000 of Taxes Paid of Southern States

	Federal Expenditures	Loans Closed	Loans Insured
Mississippi	\$4,589	\$2,718	\$262
North Dakota	3,780	931	65
Arkansas	2,685	610	317
South Dakota	3,948	1,165	129
Idaho	2,953	1,619	243
Wyoming	3,185	981	377
Alabama	2,533	823	181
New Mexico	3,772	930	225
South Carolina	2,987	731	188
Oklahoma	2,201	571	250
Average, 10 Southern states	3,263.3	1,117.9	223.7
U. S.	978	260	164

## TAXES AND TREASURY DISBURSEMENTS 195

14. This table suggests that the 10 Southern and Western states profited from Federal disbursements almost  $5\frac{1}{2}$  times as large relative to tax burdens as the 10 Northern states. The latter states received back amounts equal to about 60 per cent of the taxes borne. In loans closed, the Southern and Western states received 10 times as much relative to taxes borne as the Northern states. But in loans insured the relative total was but  $1\frac{1}{2}$  times that of the Northern states.

### 1939: TAXES BORNE AND FEDERAL DISBURSEMENTS

15. Finally, I come to a breakdown for 1939 of Federal tax incidence and value, per thousand dollars of taxes paid, of expenditures, loans closed, and loans insured for New England, for the South Atlantic, and for the East South Central states—as well as for the 10 richest and 10 poorest states. The New England states get back about two thirds in expenditures, one third in loans closed, and 37 per cent of loans insured as the country generally. Roughly the same percentages hold for the relation of the New England states and the South Atlantic states; but in relation to the East South Central, the percentages received back by New England are less than one third, one tenth, and less than one third, respectively, than Federal expenditures, loans closed, and loans insured. *In relation to 5 major Southern industrial states, New England received back in expenditures one third as much relative to taxes borne, and Connecticut, Massachusetts, and Rhode Island received back only 21, 37, and 30 per cent, respectively, as much as the Southern states.*

16. The 10 richest states, with 43.5 per cent of the income of the nation, accounted for 49 per cent of the tax incidence and received back only 59 per cent and 51 per cent as much in Federal expenditures and loans closed respectively in relation to taxes borne *vis-à-vis* the country's totals. The 10 poorest states accounted for 7.5 per cent of the taxes, 9.6 per cent of the income, and received back 2.3 as much relative to taxes borne in expenditures and 3.2 times in loans closed as the total for the country.

Federal Tax Payments and Federal Expenditures, Loans  
Closed, and Loans Insured Per Thousand Dollars  
of Taxes Paid, Fiscal 1939\*

State	Federal Tax Incidence (\$1,000)	Value, Per Thousand Dollars of Taxes Paid, of		
		Expenditures <sup>a</sup>	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
Alabama	40,293	2,533.12	922.72	181.37
Arizona	14,839	2,685.09	610.09	317.20
Arkansas	25,261	3,725.74	2,161.67	142.12
California	410,579	743.43	233.96	407.46
Colorado	42,207	1,827.49	368.90	181.60
Connecticut	123,017	436.83	46.17	76.48
Delaware	39,875	243.66	11.81	40.80
D. C.	51,866	1,579.07	82.79	74.89
Florida	81,869	821.04	242.16	273.31
Georgia	58,360	1,805.79	766.18	220.13
Idaho	12,405	2,953.33	1,618.62	243.05
Illinois	410,926	785.91	263.02	143.40
Indiana	102,132	1,359.25	261.64	264.50
Iowa	67,967	1,446.55	1,446.51	116.75
Kansas	41,918	1,956.82	546.57	215.92
Kentucky	54,106	1,749.23	322.63	163.16
Louisiana	55,925	1,783.46	585.19	173.23
Maine	33,595	561.87	125.32	59.47
Maryland	100,104	495.07	95.80	137.37
Massachusetts	246,797	759.86	92.98	45.77
Michigan	226,802	927.81	125.33	342.03
Minnesota	104,504	1,218.52	345.77	119.14
Mississippi	21,526	4,589.52	2,718.06	262.33
Missouri	135,085	1,221.02	234.04	147.50
Montana	19,881	3,061.42	1,421.81	103.11
Nebraska	36,332	1,966.31	1,109.38	152.87
Nevada	8,668	1,502.77	396.86	184.13
New Hampshire	20,297	887.72	247.62	77.55
New Jersey	236,584	577.45	131.38	179.69
New Mexico	10,289	3,772.48	929.54	225.00
New York	1,073,603	409.85	72.02	82.48
North Carolina	66,743	1,380.29	349.04	107.37
North Dakota	12,863	3,779.76	931.74	64.99
Ohio	306,565	1,060.05	106.70	151.05
Oklahoma	52,158	2,201.23	570.52	249.95
Oregon	37,345	1,575.10	588.81	204.45
Pennsylvania	473,808	731.55	75.21	97.18
Rhode Island	42,072	630.51	72.88	93.91
South Carolina	26,310	2,986.89	730.60	187.69
South Dakota	12,660	3,948.42	1,164.61	128.67
Tennessee	51,881	1,678.21	771.96	226.52
Texas	197,106	1,285.12	618.32	241.34

Sources: See text.

\* For relevant notes, see first table on 1939.

## TAXES AND TREASURY DISBURSEMENTS 197

### Federal Tax Payments and Federal Expenditures, Loans Closed, and Loans Insured Per Thousand Dollars of Taxes Paid, Fiscal 1939\* (*Continued*)

State	Federal Tax Incidence (\$1,000)	Value, Per Thousand Dollars of Taxes Paid, of		
		Expenditures <sup>a</sup>	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
Utah	13,825	2,378.52	529.40	368.39
Vermont	11,990	1,331.19	401.83	103.42
Virginia	70,433	1,015.21	143.82	211.78
Washington	65,775	1,902.15	365.76	316.15
West Virginia	41,805	1,468.13	134.29	157.49
Wisconsin	115,887	1,101.99	188.91	99.06
Wyoming	8,387	3,185.05	981.28	376.65
Total U. S. <sup>d</sup>	5,515,225	978.23	260.48	164.29

### Federal Tax Payments and Federal Expenditures, Loans Closed, and Loans Insured Per Thousand Dollars of Taxes Paid, Fiscal 1939\*

#### New England, South Atlantic, and East-South-Central States

State	Federal Tax Incidence (\$1,000)	Value, Per Thousand Dollars of Taxes Paid, of		
		Expenditures <sup>a</sup>	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
U. S. Total <sup>d</sup>	5,515,225	978.23	260.48	164.29
New England	477,968	684.92	95.71	61.65
Connecticut	123,017	436.83	46.17	76.48
Maine	33,595	761.87	125.32	59.47
Massachusetts	246,797	759.86	92.98	45.77
New Hampshire	20,297	887.72	247.62	77.55
Rhode Island	42,072	630.51	72.88	93.91
Vermont	11,990	1,331.19	401.83	103.42

Sources: See first table on 1939.

\* For relevant notes, see *ibid.*

Federal Tax Payments and Federal Expenditures, Loans  
Closed, and Loans Insured per Thousand Dollars  
of Taxes Paid, Fiscal 1939\* (*Continued*)

New England, South Atlantic, and East-South-Central States

State	Federal Tax Incidence (\$1,000)	Value, Per Thousand Dollars of Taxes Paid, of		
		Expenditures*	Loans Closed <sup>b</sup>	Loans Insured <sup>c</sup>
South Atlantic	485,499	995.25	273.66	173.44
Delaware	59,875	243.66	11.81	40.80
Florida	81,869	821.04	242.16	273.31
Georgia	58,360	1,805.79	766.18	220.13
Maryland	100,104	495.07	95.80	137.37
North Carolina	66,743	1,380.29	349.04	107.37
South Carolina	26,310	2,986.89	730.60	187.69
Virginia	70,433	1,015.21	143.82	211.78
West Virginia	41,805	1,468.13	134.29	157.49
East South Central	167,806	2,279.85	912.92	199.84
Alabama	40,293	2,533.12	922.72	181.37
Kentucky	54,106	1,749.23	322.63	163.16
Mississippi	21,526	4,589.52	2,718.06	262.33
Tennessee	51,881	1,678.21	771.96	226.52
10 Richest	2,692,225	573.84	132.88	148.17
10 Poorest	409,501	2,237.39	822.40	185.47

A STUDY OF TAXES AND EXPENDITURES FOR 1952\*

17. Obviously a study of *all* expenditures, not merely grants and aids upon which we have concentrated so far, yields somewhat different conclusions than the more limited study. The broader study includes the large volume of market transactions—in particular government purchases of goods and services. Since a large part of the purchases are manufactured products related to war, the incidence of these outlays is to be found primarily in the industrial states. Hence a broad analysis of Federal outlays reveals outlays more closely related to income,

\* What follows in this section on 1952 is primarily based on statistical materials (now in mimeographed form) by Miss Mushkin and Miss Crowther, but the arrangement and analysis is mine. I owe much to their study, which they kindly allowed me to use.



## TAXES AND TREASURY DISBURSEMENTS 199

though still greatly exceeding tax contributions of the poorer states than a study restricted to grants and aids.

18. Outlays for natural resources tend to favor the sparsely populated and on the whole the poorer states, and this generalization holds also for highway outlays and assistance programs. The poorer states also profit disproportionately from Federal loans and even guarantees. But under insurance programs, and notably OASI and Unemployment Compensation, the wealthy states seem to profit from disbursements at least equal to their share of income. They gain disproportionately, then, from government purchases inclusive of interest payments; at least proportionately from insurance programs; and lose heavily from the government programs of grants and assistance, whether administered through state or local governments or paid directly to individuals. *In a general way, it may be said that the richer states gain from market transactions and lose through grants and aids.*

### REVENUE INCIDENCE AND FEDERAL EXPENDITURES

19. In the next table, Miss Mushkin and Miss Crowther compare the incidence of revenue and of expenditures. In their analysis they estimate expenditures on a benefit and an incidence basis. Under the former the criterion is who benefits from a program (e.g., under a military program it is assumed all share equally); under the latter criterion, the test is who gets the cash poured out by the Federal Government. On a government contract, the relevant point would be where the item is produced.

20. Obviously, the results can only be roughly accurate; for all kinds of assumptions and estimates are involved. The crude figures for disbursements at least are accurate: they tell us amounts received by each state. The "benefit" disbursements require allocations according to benefits; the incidence figures tell us who profits from the disbursement, not necessarily where the contract is made.

20. In the following table, adapted from the Mushkin-Crowther study, the comparison is of revenues and intermediate expenditures—the latter an average of the benefit and incidence expenditures. It will be noted that, whereas New England accounts for 8.08 per cent of revenue, she receives but 6.175

per cent of the expenditures. Maine alone of the New England states receives as much relatively as taxes borne.

22. The Middle East states are roughly in the same position as New England, with the percentage of revenue exceeding that of expenditures by about one third. New York's revenue contributed exceeds that of its expenditures by 60 per cent.

23. The Southeast and Southwest profit greatly. Their expenditure receipts exceed their revenue by 63 and 44 per cent, respectively. Relatively, the Southeast's expenditure-revenue is more than twice that of New England. The ratio of expenditure receipts to revenues for the sparsely settled Northwest is 179 per cent. In the Central states, with large segments both industrial and agricultural, revenues borne exceed Federal disbursements by 9 per cent; and in the Far West, there is roughly a balance.

24. Variations in expenditures per capita are much greater than in revenues. In 1952, Federal tax burdens ranged from \$112 per capita in Mississippi to 9 times as much, or \$1,015, in Delaware. The range of benefit expenditures was from \$403 to \$573 per capita. In another survey where revenues and benefit expenditures are compared, the differences between New England and the Middle East, on the one hand, and the South, on the other, is much greater than in the comparison of revenues and the intermediate estimate (benefits and incidence averaged). But a comparison of revenue and expenditure on an incidence basis yields a somewhat smaller difference, the explanation being the large amounts of Federal contracts, accruing to the industrial states and reflected greatly in the incidence totals. But the ratio of expenditures to revenues for the Southeast *vis-à-vis* New England is still almost twice as great.

#### TAX BURDENS

25. A second table shows revenue burdens (somewhat more inclusive than taxes, for revenue per capita is \$435 and taxes \$412). The per cent of U. S. average varies from 29 per cent for Mississippi to 238 for Delaware. Whereas New England's revenue incidence is \$577 per capita and the Middle East \$583, the averages for the Southeast, Southwest, and Northwest are \$239, \$317, and \$332, respectively.

# TAXES AND TREASURY DISBURSEMENTS 201

Estimated Incidence of Federal Cash Revenue and Intermediate Estimate of Federal Expenditures,  
by State and Region, Fiscal Year 1952

	Revenue <sup>a</sup> Incidence (millions)	Intermediate Expenditure Estimate (millions) <sup>b</sup>	Excess Revenues (+) or Expenditures (-) (millions)	Per Cent Distribution of Excess of Revenues <sup>c</sup>	Per Cent Distribution	
					Revenue Incidence	Estimated Expenditures
Continental U. S.	\$67,274	\$66,660	\$ + 613	100.0	100.000	100.000
New England	5,436	4,116	+ 1,320		8.080	6.175
Connecticut	1,502	1,065	+ 437	4.6	2.232	1.598
Maine	348	349	- 1		.518	.523
Massachusetts	2,758	2,057	+ 701	7.4	4.100	3.085
New Hampshire	229	185	+ 44	.5	.341	.277
Rhode Island	458	332	+ 126	1.3	.681	.498
Vermont	140	129	+ 12	.1	.209	.193
Middle East	21,106	15,949	+ 5,157		31.374	23.925
New York	10,672	6,623	+ 4,048	42.5	15.863	9.936
Southeast	7,751	12,628	- 4,877		11.522	18.945
Alabama	549	1,204	- 655		.816	1.806
Georgia	828	1,292	- 465		1.230	1.938
North Carolina	950	1,293	- 343		1.412	1.939
South Carolina	404	889	- 485		.601	1.334
Tennessee	740	1,499	- 759		1.100	2.249
Southwest	3,783	5,430	- 1,647		5.623	8.146
Texas	2,716	3,576	- 860		4.038	5.365
Central	18,575	16,924	+ 1,651	15.5	27.611	25.388
Illinois	5,089	3,610	+ 1,479		7.565	5.416
Northwest	2,712	3,722	- 1,010		4.032	5.583
Far West	7,911	7,891	+ 20		11.759	11.838

\* See "Measurement of the Distribution of Federal Expenditures and Revenues, by State" for explanatory notes on allocation of incidence among states.

<sup>b</sup> Based on Mushkin-Crowther study with total cash payments to the public adjusted to a daily Treasury Statement basis.

<sup>c</sup> Represents the percentage distribution of positive amounts only shown in the column on excess incidence.

Note: Amounts may not add to totals because of rounding.

Estimated Per Capita Federal Revenue and Tax Incidence,  
by State and Region, Fiscal Year 1952

Region and State	Per Capita Revenue Incidence	
	Amount	Per Cent of U. S. Average
Continental U. S.	\$435	100
New England	577	133
Connecticut	725	167
Maine	390	90
Massachusetts	582	134
New Hampshire	430	99
Rhode Island	570	131
Vermont	378	87
Middle East	583	134
New York	711	163
Southeast	239	55
Alabama	177	41
Georgia	236	54
North Carolina	228	52
South Carolina	181	43
Tennessee	226	52
Southwest	317	73
Texas	334	77
Central	454	104
Illinois	572	131
Northwest	332	76
Far West	510	117

In the next table, the material for states with incomes above average and those with incomes below average are given. The former (20 states) bore 72 per cent of the burden of Federal revenues; but profited only from 57.3-61.5 per cent of the expenditures, depending upon the manner of measuring expenditures. The 29 states with incomes below average accounted for 28 per cent of the revenue burden and profited from 38.5-42.7 per cent of expenditures. Relatively poor states received 75 per cent more in relation to revenues contributed than the rich states. This division of states with above or below average income minimizes the differences. A comparison of such wealthy states as New York and Connecticut with such states as Alabama and Tennessee reveals much greater differ-

# TAXES AND TREASURY DISBURSEMENTS 203

Estimated Distribution of Federal Expenditures (3 Illustrative Estimates) and Revenue Incidence,  
by State Per Capita Income  
(Amounts in Millions)

States Ranked by 1951-52 Per Capita Income	I Intermediate Illustration	II Benefit Illustration	III Expenditure Incidence Illustration	Revenue Incidence
Per cent of continental U. S.	100.0	100.0	100.0	100.0
States with income above U. S. average	59.8	57.3	61.5	72.0
States with income below U. S. average	40.2	42.7	38.5	28.0
20 States, total	\$40,325	States with Per Capita Income Above U. S. Average \$39,188	\$40,866	\$48,455
Selected States				
Delaware	166	149	181	349
Connecticut	1,077	852	1,278	1,502
New York	6,698	6,578	6,421	10,672
Illinois	3,651	3,745	3,462	5,089
Massachusetts	2,080	2,096	2,016	2,758
Rhode Island	335	357	308	458
29 States, total	27,085	States with Per Capita Income Below U. S. Average 29,188	25,585	18,817
Selected States				
New Hampshire	187	229	146	229
Texas	3,617	3,721	3,593	2,716
Idaho	279	315	247	161
Maine	353	380	330	348
Vermont	130	161	103	140
Georgia	1,307	1,519	1,150	828
Tennessee	1,516	1,510	1,569	740
South Carolina	899	915	920	404
North Carolina	1,307	1,676	1,001	950
Alabama	1,218	1,387	1,099	549
Mississippi	757	968	585	275

ences. An interesting point is that the 3 poorer New England states (New Hampshire, Vermont, and Maine) contribute \$717 million and receive back only \$670 million (the intermediate estimate). This is unusual for states with less than average income. Rhode Island, a state experiencing difficult transitional problems, pays out \$123 million, or 37 per cent, more than she gets back. Connecticut and Massachusetts pay out \$1,103 million more than they receive back, and New England, \$1,273 million.

#### DISTRIBUTION OF FEDERAL PAYMENTS BY TYPES

27. Federal income payments as classified by the Department of Commerce exclude purchases of goods and services. The next table suggests that New England's share of Federal income payments roughly corresponds to its share of income; but these Federal payments are much below ( $4\frac{2}{3}$  per cent of the total) its income share ( $6\frac{1}{2}$  per cent) of military and civilian pay and somewhat above in payments from trust funds and other. In general, Federal income payments are heavy for the Southeast. Thus, though her share of income is about twice that of New England, her share of these Federal income payments is  $3\frac{1}{2}$  times as great; and the Southwest, with about the same percentage of income as New England, receives about 80 per cent more in these payments.

28. Another table giving the facts for military procurement and construction contracts further clarifies the issues. In this field—and especially for the years 1950–54 (July, 1950–March, 1954)—New England's experience has been satisfactory. She received 8 per cent, or \$8.1 billion, of \$101 billion of military procurement and construction contracts. Here her total exceeds the Southeast by almost 20 per cent and the Southwest by about two thirds. Connecticut, in particular, is in a favorable position. Her receipts amount to 4.3 per cent of the nation's total as compared to but 2.6 per cent for Massachusetts. (In Federal Government income payments, Connecticut's proportion was 0.9 per cent and Massachusetts 3.0 per cent.)

29. For Walsh-Healey contracts (military items are excluded) New England's record is even better. She accounts for 12.7 per cent of \$11 billion of these contracts for 1952, with Con-

necticut capturing 5.8 per cent, Massachusetts 4.3 per cent, and Rhode Island and Maine each 1 per cent.

30. Once the measurements are based on the place of production rather than that of the consummation of contract, the concentration of business is greatly reduced. New England's share is reduced from 8 (military prime) and 12.7 (Walsh-Healey) to 7.5 per cent. The reduction is large for Connecticut, and Massachusetts gains. Large relative gains are to be noted for the Southeast (6.8 and 11.1, respectively, to 11.5) and the Southwest. New York loses substantially.

31. Finally, we present a table which shows Federal grants to states and localities for 1949-51. More than \$2 billion are distributed. The amounts tend to be larger on a per capita basis as incomes decline: \$13.01 for the high income group, \$15.65 for the middle income group, and \$17.56 for the low income group. In relation to income, the differences are even greater. But results vary for different states. Thus, Nevada, a high income state, received 2.2 per cent of income, Connecticut 0.6 per cent, Massachusetts 0.9 per cent. In the low income group, Mississippi received 2.4 per cent and Vermont 1.3 per cent. For assistance payments, the largest item included, the percentage of income varied from 0.4 per cent for New Jersey to 2.8 per cent for Louisiana.



Federal Government Income Payments, Calendar Year 1952<sup>a</sup>  
(In millions)

State and Region	Total Federal Income Payments	Military and Civilian Pay <sup>b</sup>	Payments from Trust Funds and Other <sup>c</sup>	Public Assistance Grants <sup>d</sup>
Continental U. S.	\$27,282.5	\$12,741.0	\$13,288.2	\$1,253.3
New England	1,606.7	593.4	936.9	76.4
Connecticut	242.2	54.0	178.8	9.4
Maine	171.3	82.4	81.3	7.6
Massachusetts	907.8	355.2	505.0	47.6
New Hampshire	69.7	16.2	50.0	3.5
Rhode Island	164.5	70.7	88.4	5.4
Vermont	51.2	14.9	33.4	2.9
Middle East	6,999.0	3,295.0	3,514.8	189.2
New York	2,509.3	908.1	1,503.8	97.4
Southeast	5,509.5	2,811.7	2,412.3	185.5
Alabama	593.4	257.7	261.6	24.1
Georgia	638.7	358.8	244.5	35.4
North Carolina	475.5	206.1	247.0	22.4
South Carolina	349.7	189.0	145.7	15.0
Tennessee	482.9	203.5	252.6	26.8
Southwest	2,290.8	1,268.2	888.3	134.3
Texas	1,499.4	843.9	583.7	71.8
Central	5,653.1	1,865.8	3,483.4	303.9
Illinois	1,359.4	538.1	765.2	56.1
Northwest	1,517.5	739.8	699.0	78.7
Far West	3,705.9	2,167.1	1,353.5	185.3

<sup>a</sup> All figures are from Office of Business Economics, Department of Commerce, except those on public assistance, which are from "Social Security Bulletin," September 1953, p. 61.

<sup>b</sup> Includes net military pay and gross wages and salaries of civilian employees less contributions for disability insurance and retirement.

<sup>c</sup> Includes interest payments to individuals, benefits paid from social insurance trust funds (old-age and survivors insurance, railroad retirement, railroad unemployment insurance, railroad cash sickness, Civil Service and other Federal retirement programs, State unemployment insurance), veterans' subsistence, interest payments on veterans' loans, military reserve pay, adjusted service bonds, military retirement pay, allowances and allotments, mustering out pay, terminal leave pay, national service life insurance special dividends, payments by War Claims Commission, veterans' indemnity payments, and payments to farmers (Federal payments classified by the Office of Business Economics as income to self-employed farmers, including some \$30 million classified as rental income).

<sup>d</sup> Includes Federal share for assistance and administration of old-age assistance, aid to dependent children, aid to the blind, aid to the permanently and totally disabled, and general assistance programs.

Value of Military Procurement and Construction Contracts (Prime Contracts)  
Awarded in the United States, by Region and State, Fiscal Year 1952  
and July 1950-March 1954

Region and State	Fiscal Year 1952				July 1950-March 1954			
	Amount* (in thousands)	Per Cent Distribution <sup>b</sup>	Per Capita <sup>a</sup>		Amount <sup>d</sup> (in thousands)	Per Cent Distribution <sup>b</sup>	Per Capita <sup>a</sup>	
			Amount	Rank			Amount	Rank
Total awarded, continental U. S. \$42,000,815					\$110,249,786			
New England	2,263,008	5.9	\$240	—	8,101,816	8.0	\$ 860	—
Connecticut	963,354	2.5	465	4	4,302,010	4.3	2,076	1
Maine	138,697	.4	155	20	368,611	.4	413	20
Massachusetts	920,378	2.4	194	14	2,651,660	2.6	559	16
New Hampshire	62,755	.2	118	24	198,332	.2	372	23
Rhode Island	146,035	.4	182	16	467,234	.5	581	14
Vermont	31,789	.1	85	29	113,969	.1	306	26
Middle East	11,579,166	30.2	320	—	28,846,545	28.6	797	—
New York	6,246,809	16.3	416	6	15,629,984	15.5	1,041	7
Southeast	2,594,944	6.8	80	—	6,857,676	6.8	211	—
Alabama	217,975	.6	70	32	598,563	.6	193	34
Georgia	245,301	.6	70	33	1,337,140	1.3	382	22
North Carolina	427,963	1.1	103	25	862,430	.9	207	33
South Carolina	177,982	.5	82	30	385,586	.4	178	35
Tennessee	296,273	.8	90	28	722,924	.7	220	32
Southwest	1,443,835	3.8	121	—	4,787,285	4.7	401	—
Texas	1,298,475	3.4	160	19	3,500,878	3.5	431	19
Central	13,197,947	34.4	323	—	30,408,824	30.1	744	—
Illinois	1,733,937	4.5	195	13	4,913,670	4.9	552	17
Northwest	592,624	1.5	73	—	3,035,288	3.0	371	—
Far West	6,657,365	17.4	430	—	18,899,332	18.7	1,219	—

\* Data from *Munitions Board Report 3B*, 15 October 1952; *Military Prime Contracts*, by State, July 1950-June 1952.  
<sup>b</sup> Amounts may not add to totals because of rounding.

\* Based on average of Census Bureau estimates of population (Series P-25, No. 84) for July 1, 1951 and July 1, 1952.

<sup>d</sup> Data from Department of Defense, Office of Assistant Secretary of Defense (Supply and Logistics), 15 June, 1954; *Military Prime Contracts*, by State, July 1950-March 1954, table 1.

Unclassified Contracts Awarded Subject to the Walsh-Healey  
Public Contracts Act During Fiscal Year 1952,  
by State and Region of Manufacture

Region and State	Amount <sup>a</sup> (in thousands)	Per Cent <sup>b</sup>	Per Capita <sup>c</sup>	
			Amount	Rank
Continental U. S.	\$10,966,552	100.0	\$ 71	—
New England	1,396,431	12.7	148	—
Connecticut	637,679	5.8	308	1
Maine	107,727	1.0	121	5
Massachusetts	473,729	4.3	100	8
New Hampshire	55,677	.5	104	7
Rhode Island	108,847	1.0	135	4
Vermont	12,772	.1	34	30
Middle East	3,079,344	28.1	85	—
New York	1,178,352	10.7	78	13
Southeast	1,220,529	11.1	38	—
Alabama	104,397	1.0	34	29
Georgia	128,988	1.2	37	25
North Carolina	126,875	1.2	30	31
South Carolina	124,522	1.1	57	18
Tennessee	171,366	1.6	52	20
Southwest	304,611	2.8	26	—
Texas	219,657	2.0	27	35
Central	3,781,107	34.5	92	—
Illinois	787,500	7.2	89	9
Northwest	131,144	1.2	16	—
Far West	1,053,386	9.6	68	—

<sup>a</sup> Data from U. S. Department of Labor, *1952 Annual Report of the Wage and Hour and Public Contracts Divisions*, pp. 61-62.

<sup>b</sup> Amounts may not add to totals because of rounding.

<sup>c</sup> Based on average of Census Bureau estimates of population (Series P-25, No. 84) for July 1, 1951 and July 1, 1952.

Percentage Distribution of Federal Contract Awards and  
Estimated Production Impact of Military Purchases,  
by Region and State

Region and State	Military Prime Contracts, 1950-54	Contracts under Walsh-Healey Act, 1952	Estimated Military Purchases, 1952
Continental U. S.	100.0	100.0	100.0
New England	8.0	12.7	7.5
Connecticut	4.3	5.8	3.2
Maine	.4	1.0	.5
Massachusetts	2.6	4.3	3.2
New Hampshire	.2	.5	.2
Rhode Island	.5	1.0	.4
Vermont	.1	.1	.1
Middle East	28.6	28.1	26.1
New York	15.5	10.7	10.1
Southeast	6.8	11.1	11.5
Alabama	.6	1.0	1.4
Georgia	1.3	1.2	1.1
North Carolina	.9	1.2	1.0
South Carolina	.4	1.1	.5
Tennessee	.7	1.6	1.3
Southwest	4.7	2.8	6.2
Texas	3.5	2.0	4.6
Central	30.1	34.5	31.7
Illinois	4.9	7.2	5.7
Northwest	3.0	1.2	3.9
Far West	18.7	9.6	13.1

Note: Amounts may not add to totals because of rounding.

Per Capita Federal Grants to States and Localities, by State and Purpose, Fiscal Year 1952<sup>a</sup>

	Average Per Capita Income, 1949-51	Per Capita Grants							All Other <sup>e</sup>
		Total	Assistance Payments and Administration <sup>b</sup>	Employment Security Administration <sup>c</sup>	Health Services <sup>d</sup>	Other Welfare Services <sup>e</sup>	Education <sup>f</sup>		
Continental U. S.	\$1,449	\$14.94	\$7.63	\$1.18	\$1.16	\$ .72	\$ .71	\$3.54	
High-income group		13.01	6.92	1.47	.72	.53	.61	2.77	
New York	1,871	10.85	5.94	1.87	.42	.42	.17	2.03	
Connecticut	1,792	10.85	4.97	1.37	.81	.66	.41	2.63	
Illinois	1,771	11.65	6.05	1.06	.65	.53	.52	2.84	
Massachusetts	1,596	14.02	9.12	1.78	.76	.49	.22	2.55	
Rhode Island	1,554	17.72	6.66	2.22	1.60	.61	.85	5.78	
Middle-income group		15.65	7.68	1.01	1.21	.67	.72	4.35	
New Hampshire	1,319	15.29	5.80	1.81	1.60	.74	.59	4.75	
Texas	1,296	17.83	8.37	.85	1.45	.71	.98	5.48	
Low-income group		17.56	8.84	.87	1.87	1.14	.88	3.96	
Vermont	1,208	16.26	7.66	1.23	1.44	1.05	.69	4.18	
Maine	1,197	16.95	8.29	1.23	1.64	.75	.57	4.47	
Georgia	978	19.00	9.66	.81	1.96	1.34	1.63	3.61	
Tennessee	965	14.78	7.62	.88	1.42	1.17	.41	3.28	
North Carolina	953	12.56	4.99	.83	1.80	1.17	.46	3.32	
South Carolina	877	15.43	6.42	1.11	2.18	1.38	.69	3.66	
Alabama	853	16.14	7.64	.88	2.39	1.34	.51	3.37	

<sup>a</sup> From *Social Security Bulletin*, June 1953.<sup>b</sup> Old age assistance, aid to dependent children, aid to the blind, and aid to the permanently disabled.<sup>c</sup> Unemployment insurance and employment service administration.<sup>d</sup> Maternal and child health services, services for crippled children, general public health services, venereal disease, tuberculosis, heart disease, and cancer control, mental health activities, hospital survey and construction, and water pollution control.<sup>e</sup> Child welfare services, vocational rehabilitation, State and Territorial homes for disabled soldiers and sailors, and school lunch programs.<sup>f</sup> Colleges for agriculture and mechanic arts, vocational education, education of the blind, State marine schools, school survey and construction, and maintenance and operation of schools in certain areas.<sup>g</sup> Agricultural experiment stations and extension work, cooperative projects in marketing, forestry cooperation, removal of surplus agricultural commodities, commodities donated by the Commodity Credit Corporation, wildlife restoration, annual contributions to public housing agencies, Federal airport program, regular and emergency highway construction, and civil defense grants.

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### FEDERAL DISBURSEMENTS AND NATIONAL INCOME, 1954

32. In a master table for 1954, we have compared Federal disbursements in New England relative to New England's income and relative to her Federal tax burden; and the disbursements relative to tax burdens for New England in comparison with similar ratios for the United States, South Atlantic and East South Central states, and New York, as an example of an additional Northern state. In this study, I include the total of each of 8 categories, inclusive of the smaller items, but comparisons of individual programs are limited to the 75 costing \$10 million or more in 1954. The original material includes 140 programs. In this master table, I also compare the disbursements in the 10 richest and the 10 poorest states, both relative to incomes and taxes borne.

33. Here are some of the results to be gleaned from this master table:

*Federal disbursements in New England as a percentage of New England's income.* In 18 out of 75 programs, New England gains in excess of its proportion of income. In the category totals, percentage of disbursement exceeds percentage of income only in D (grants and payments to individuals) and G (non-tax financed Federal insurance).

#### Programs Costing More Than \$10 Million, New England's Share in Federal Disbursements and in the National Income, 1954

	Percentage Share in Federal Disbursements Was Greater Than Percentage Share in NI in:
Aid to states and local government	8 out of 25 programs
Loans to states and local government	0 out of 1 program
Projects within states	0 out of 8 programs
Grants and payments to individuals and groups	4 out of 13 programs
Loans to individuals and groups	0 out of 8 programs
Loan guaranties and insurance	0 out of 1 program
Non-tax financed insurance payments	1 out of 1 program
Salaries, services and procurement	5 out of 18 programs

34. For Category A (grants to states and local units), New England received in Federal disbursements only 81 per cent as much as might be expected from her relative income. The

total amount spent by the Federal Government in this category was close to \$4 billion.

35. Under the Federal highway program (\$532 million), New England received only 72.1 per cent of what might be expected on the basis of her relative income; from old age assistance (\$957 million program), 88 per cent; from grants for aid to dependent children (\$360 million), New England's relative receipts were 75 per cent. The only substantial programs in this category where New England received amounts in excess of her relative income position was the annual contributions to state and local authorities of the Public Housing Administration (\$37 million program), with New England receiving 161 per cent relative to her income position; and the grants to states of the Bureau of Employment (\$198 million program), where New England received 120 per cent of the amount suggested by relative income.

35a. Under B (loans to state and local authorities), New England again does not fare too well. Its relative share of loans in slum clearance is 47 per cent (again, 100 is the figure suggested by relative income).

36. Of the 8 projects listed under C (projects within states) and accounting for \$944 million, New England's total is only 9 per cent in relation to her relative income, or one-eleventh of what might be expected from relative income. (New England received 6/10 of 1 per cent of disbursements.) Under the largest program in this category (civil projects of Army Corps of Engineers), accounting for \$532 million, New England received 0.62 per cent, or 9 per cent of the amount expected from her relative income.

37. In Category D, New England profited from disbursements in only 4 out of 13 programs in amounts exceeding her share of national income. But for the whole category (total grants and payments to individuals and groups) Federal disbursements were \$9,824 million and New England received 112 per cent of the amount indicated by her relative income.

38. The explanation of these favorable results for New England lie largely in the importance of insurance programs—the high incomes and wide coverage in Old Age and Survivors Insurance (OASI), the wide coverage under unemployment



## TAXES AND TREASURY DISBURSEMENTS 213

insurance (and high incidence of unemployment), and relatively large veterans' pensions are relevant here.

Program	Amount of Disburse- ments (\$ million)	New England Receipts, % of Total	% Received by N. E. Relative to New England's Income
Veterans' Administration			
Pensions	2,368	7.25	109.5
Bureau of Employment Security:			
Withdrawals by States	2,015	7.68	116.0
Bureau of Old Age and Survivors Insurance: Benefits Paid	3,633	9.11	117.7

39. The largest relative gains of New England in this category are to be found in the item, Public Health Services, National Institute of Health Fellowships, Grants and Trainee Rewards. New England's share relative to her relative income is 251 per cent. The program of \$43 million is a small one; but New England's favorable position is explained by her eminence in education and health. In other important programs, Railroad Retirement, Unemployment and other benefits (\$648 million), Conservation Programs Payments to Farmers (\$172 million), Veterans' Benefits, Readjustment Benefits under Public Laws 364 and 500 (\$574 million), New England's share was relatively low compared to her share of income: 52, 24, and 77 per cent, respectively.

40. I repeat that New England's favorable position in this category is explained primarily by insurance programs where an industrial region profits (?) from higher coverage and more unemployment. The payments are related more directly to what is paid than is true generally of Federal disbursements.

41. In Category E (loans to individuals and groups), which amounted to \$6,173 million in 1954, New England's share was but 1.26 per cent. In every instance, New England's record was poor. Thus, in the 5 major programs, V. A. Direct Loans to Veterans (\$118 million), Farm Credit Administration, Loans Closed by Agencies under FCA (\$2,158 million), Rural Electrification Loans (\$236 million), Department of Agriculture, Farmers' Home Administration Direct Loans (\$280 million),

and Commodity Credit Corporation Non-recourse Loans (\$3,305 million), New England's share relative to her ratio of income was 24, 47, 1, 27, and 1 per cent, respectively.

42. Under F (loans guaranteed and insured), the amounts involved were \$4,934 million. New England received 90 per cent of the amount indicated by her relative income. For the V. A. guarantee of loans to veterans (\$1,855 million), New England's share on this criterion was 120 per cent; but of the housing loans insured by the Housing Administration (\$3,069 million), New England received but 60 per cent of the amounts suggested.

43. Of \$3,663 million paid out in salaries by the Federal Government (Category 3A), New England received 88 per cent as much as is indicated by her relative income. The percentages vary from 3 per cent (Agricultural Research) to 130 per cent (Army National Guard Payments). For the largest item, Post Office, Mail Delivery and Collection (\$1,619 million), New England's relative percentage was 105.

44. For the \$17.8 billion of expenditures in all, New England received 6.36 per cent, or 96 per cent of the amounts indicated by her income. Without insurance payments, New England's share is, of course, much smaller, and notably in grants to state and local governments and projects within states.

45. Of the \$6.2 billion of loans closed, New England's share was especially low: 19 per cent of the expected level. Of the \$4.934 million loans insured, New England received 90 per cent of the total expected.

#### DISBURSEMENTS IN RELATION TO TAXES BORNE

46. The table which follows summarizes the relation of New England to the United States. For 75 substantial programs, the ratio of Federal disbursements in New England per \$1,000 of taxes exceeds that of the nation in only 6 programs, is up to 25 per cent less than the national ratio for 16 programs, 25-50 per cent less for 16 programs, and more than 50 per cent less for 37 programs.

47. Since New England's Federal tax burden as a percentage of the national tax burden exceeds her percentage of the national income, it would be expected that a comparison of Federal disbursements in New England relative to New England's tax

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## Programs Costing More than \$10 Million Federal Disbursements per \$1,000 of Taxes—New England and the United States

	More than Those in U. S.	Federal Disbursements in New England per \$1,000 of Taxes Were:		
		Less than those in U. S. by:		
		25% or Less	26-50%	51% or More
Aid to states and local government	2	8	8	7
Loans to states and local government	—	—	1	—
Projects within states	—	—	1	9
Grants and payments to individuals and groups	2	2	3	6
Loans to individuals and groups	—	—	—	8
Loan guarantees and insurance	1	—	1	—
Non-tax financed insurance payments	—	1	—	—
Salaries, services and procurement	2	5	2	9
Additions of above	7	16	16	39

burdens in the nation would show an even less favorable position for New England than was revealed in the earlier comparisons of disbursements on the basis of relative incomes.

48. Hence the percentages in Column 4 of the master table are invariably lower than those in Column 3. The only instances under A (grants to states and localities) where a percentage in excess of 100 is revealed for New England is Housing, Annual Contributions to State and Local Authorities (138 per cent) and Bureau of Employment Security, Grants to States (103 per cent). For all grants to states and localities, New England's percentage, as indicated by the ratio of Federal disbursements in New England to taxes borne by New England, is only 69.

49. The only large program where, on this criterion, New England shows a percentage in excess of that suggested by the relation of disbursements and taxes borne are benefits paid under OASI (118 per cent).

50. On the basis of comparisons of disbursements and taxes, New England also receives more than 100 per cent in the category Housing Loans (120). But for all loans her total is reduced to 77 per cent. In the salary category, her percentage for the total on this criterion is 75, and only in V. A. Construction, etc., of Hospital and Domiciliary Facilities and Army National

Guard is a figure in excess of 100 per cent reached (109 and 111, respectively).

51. For all expenditures, the percentage is 82 per cent of what would be expected on the basis of disbursements in New England relatively to taxes borne; for loans closed, 16 per cent; and for loans insured, 77 per cent. Allow me to add that the relative disbursements to taxes borne is higher in this year for New England than over a longer span.

TAXES AND DISBURSEMENTS, COMPARISON OF NEW ENGLAND,  
THE NATION, AND THE SOUTH

52. Useful comparisons are those between New England, on the one hand, and the South Atlantic and the East South Central states, on the other. Again, the comparison is of Federal disbursements received and taxes borne. In relation to the South Atlantic states, New England's receipts relative to taxes borne are less than the South Atlantic's in 69 out of 75 instances. (In 46 programs the figure for New England is more than 50 per cent below that of the South Atlantic states. In relation to the East South Central states, New England's percentage is higher in only 3 out of 75 instances and more than 50 per cent less in 57 instances.)

Programs Costing More than \$10 Million  
Federal Disbursements per \$1,000 of Taxes—New England  
and South Atlantic

	Federal Disbursements in New England per \$1,000 of Taxes Were:			
	More than Those in S. A.	Less than those in S. A. by:		
		25% or Less	26-50%	51% or More
Aid to states and local government	—	3	5	16
Loans to states and local government	1	—	—	—
Projects within states	—	—	1	5
Grants and payments to individuals and groups	3	—	2	7
Loans to individuals and groups	—	—	—	8
Loan guarantees and insurance	1	—	—	1
Non-tax financed insurance payments	—	—	1	—
Salaries, services and procurement	1	3	5	9
Additions of above	6	6	14	46

# TAXES AND TREASURY DISBURSEMENTS 217

## Programs Costing More than \$10 Million Federal Disbursements per \$1,000 of Taxes—New England and East South Central

	Federal Disbursements in New England per \$1,000 of Taxes Were:			
	More than Those in E. S. C.	Less than those in E. S. C. by:		
		25% or Less	26-50%	51% or More
Aid to states and local government	—	—	4	20
Loans to states and local government	—	—	—	1
Projects within states	—	—	—	6
Grants and payments to individuals and groups	1	1	1	8
Loans to individuals and groups	—	—	—	8
Loan guarantees and insurance	1	—	1	2
Non-tax financed insurance payments	—	—	—	1
Salaries, services and procurement	1	—	4	11
Additions of above	3	1	10	57

53. It is only necessary to show the relation of disbursements to taxes borne for New England relative to the other two groups of states. (A total of 100 means that New England's receipts from Federal disbursements relative to taxes borne are equal to those of the other section; a score of 50, that New England receives only half as much relatively.)

## Disbursements in Re Taxes, 1954

	Amounts Involved (\$ million)	New England in Re			New York in Re U. S.
		United States	South Atlantic	E. S. Central	
1. Grants to states and local units	2,958	69	49	28	44
2. Projects within states	944	8	13	3	6
3. Grants and payments to individuals	9,824	95	83	53	72
4. Total expenditures	17,799	82	68	37	63
5. Total loans closed	6,193	16	17	6	10
6. Loans insured	4,934	77	74	67	69

54. It is clear that New England received much less back for each dollar of taxes paid than the Southern states; and if the insurance payments are eliminated, the differences are striking.

See, for example, Rows 1 and 2 which give the major expenditures other than salaries and payments to individuals (largely insurance). Rows 1 and 2 are, in fact, the genuine Federal subsidies. New England's relative position is especially unfavorable in the Federal loan categories: in relation to taxes borne, she receives back but one-sixth as much as the East South Central states. In other words, the South and West are being built up with a considerable use of Federal funds.

#### NEW YORK

55. Perhaps a word should be said about other Northern states. In the last table, I inserted figures for New York State. It will be noted that Federal disbursements in New York relative to taxes borne are even lower relative to the national ratio than for New England relative to the national. For grants to states and local units, the New York figure is 44 per cent as compared with 69 for New England; for grants and payments to individuals, 72 as compared with 95 for New England; and for all expenditures, 63 as against 82. The explanation is partly higher incomes in New York and a heavier tax burden.

56. In some of the important programs, the percentage for New York varies from that for New England to an extent that suggests smaller or larger participation in a particular program—aside from the differences in tax burdens. As might be expected, the relevant figure for removal of surplus commodities was 42 (91 for New England); for highways, 36 (62 for New England); for Old Age Assistance, only 29 (75 for New England); for dependent children, 71 (64 for New England); for V. A. Pensions, 59 (94 for New England); for Railroad Retirement benefits, 47 (44 for New England); for Employment Security benefits, 91 (New England, 91); for OASI, 78 (New England, 118); for postal collections, etc., 100 (New England, 89).

#### TEN RICHEST AND TEN POOREST STATES

57. For the year 1954, the ten richest states profited from Federal disbursements in relation to the ten poorest states as follows: 240 per cent as much from expenditures, 77 per cent in loans closed, and 548 per cent in loans insured. But since the income of the rich states was more than 4 times that of the

## TAXES AND TREASURY DISBURSEMENTS 219

poor states, when disbursements are related to incomes, the respective figures become 58, 19, and 132; and when related to taxes borne, 42, 14, and 97 per cent are the totals. In other words, the richest states received only 2/5 as much from Federal expenditures and 1/7 in loans closed as might be indicated by relative taxes borne. The rich states, primarily states in the Northeast and the Middle West, receive back relatively little compared to what they pay in.

58. That the richest states get back much less than they put in might be expected. Of 75 programs, in only 3 (aside from one guarantee program) do the receipts exceed the taxes borne relatively; and these are unimportant programs.

59. Here are some details on important programs and totals which underline these conclusions. (See table on 10 Richest and 10 Poorest States.)

60. In a table following the above we compare the totals for 1953 and 1954 as well as the figures for the more important programs. It will be noted that though there are differences in the two years for the individual programs the summary figures show relatively small differences in the two years.

### Master Table

#### Programs Costing More Than \$10 Million—1954

Headings of columns on following pages:

- (I) Total cost in millions of dollars
- (II) Disbursements in New England as a per cent of total program
- (III) 
$$\frac{\text{Disbursements in New England}}{\text{Total Program}} \div \frac{\text{New England Income}}{\text{United States Income}}$$
- (IV) 
$$\left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ New England } \div \left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ United States}$$
- (V) 
$$\left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ New England } \div \left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ South Atlantic states}$$
- (VI) 
$$\left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ New England } \div \left[ \frac{\text{Disbursements}}{\$1,000 \text{ of Taxes}} \right] \text{ East South Central states}$$
- (VII) Disbursements in 10 richest states  
Disbursements in 10 poorest states
- (VIII) 
$$\left[ \frac{\text{Disbursements}}{\$1,000 \text{ Taxes}} \right] 10 \text{ richest states } \div \left[ \frac{\text{Disbursements}}{\$1,000 \text{ Taxes}} \right] 10 \text{ poorest states}$$
- (IX) 
$$\left[ \frac{\text{Disbursements in 10 richest states}}{\text{Disbursements in 10 poorest states}} \right] \div \left[ \frac{\text{Income in 10 richest states}}{\text{Income in 10 poorest states}} \right]$$

Note: For full titles of programs see pp. 228-30.



Programs (brief titles):									
A. <i>Aid to State &amp; Local Governments</i>									
I	II	III	IV	V	VI	VII	VIII	IX	
A1 Civil Defense	11.5	6.27	.947	.8333	.8824	.7143	7.0925	1.2353	1.7093
A2 Slum Clearance grants	11.6		N. E.	= nil, ESC	= nil, 10 poorest states	= nil.			
A3 Public Housing Contribution	36.9	10.67	1.612	1.3793	.5634	.2867	.7714	.1348	.1859
A4 Ag. Experiment Stations	12.7	7.84	1.185	1.0000	.5263	.3175	.7981	.1356	.1923
A5 Ag. Extension Work	3.8	3.18	.480	.4167	.2083	.0939	.5043	.0914	.1215
A6 Shared Revenue from Forest Funds	18.8	0.42	.063	.0667	.1429	.0606	3.3625	.6061	.8104
A7 Dept. Ag. School Lunch Program	78.0	4.69	.709	.6016	.2972	.1520	.8138	.1451	.1961
A8 Dept. Ag. Surplus Commodities	151.4	7.03	1.062	.9076	.5347	.3073	1.2160	.2155	.2931
A9 Civil Airport Grants	16.6	6.67	1.008	.8462	.7586	.5116	2.0714	.3750	.4992
A10 Air Highways	531.8	4.77	.721	.6168	.5438	.2322	1.6821	.2977	.4054
A11 Office Ed. Vocational Ed.	24.6	5.48	.820	.6923	.4030	.2213	1.1664	.2110	.2811
A12 School District Grants	65.2	4.99	.754	.6471	.3350	.4783	3.4209	.6058	.8244
A13 School Construction	103.9	1.00	.151	1.288	.0465	.0528	1.5468	.2745	.3728
A14 Office Ed. Vocational Rehabilitation	22.6	3.82	.577	.4857	.1977	.2152	1.2360	.2212	.2979
A15 Gen. Health Assistance, etc.	22.2	5.34	.807	.6857	.3478	.2069	1.0717	.1869	.2583
A16 Hospital Construction	84.0	3.73	.564	.4848	.2481	.1187	.7424	.1312	.1789
A17 Old Age Assistance	957.4	5.83	.881	.7527	.6718	.3370	1.5938	.2820	.3841
A18 Dept. Health—grants for disabled	73.8	6.92	1.046	.8966	.4976	.7273	1.4850	.2613	.3579
A19 Dept. Health—grants to blind	37.0	3.82	.577	.5000	.2990	.1921	1.4659	.2617	.3533
A20 Dept. Health—Aid Dependent Children	360.2	4.98	.752	.6431	.3952	.2289	1.6017	.2834	.3860
A21 Dept. Health—Child Health Service, etc.	11.2	6.88	1.040	.8889	.4000	.2286	.7208	.1290	.1737
A22 Dept. Health—services for crippled children	10.1	7.16	1.082	.9375	.4412	.2419	.7333	.1296	.1767
A23 Payments for mineral leasing	26.1		N. E.	= nil.			80.4255	12.0000	19.3825
A24 Fish and Wild Life Service	15.4	3.80	.574	.5000	.5714	.2791	1.5631	.2683	.3767
A25 Employment Security Grants	198.1	7.94	1.200	1.0257	.9969	.7185	3.7522	.6644	.9043
Total	2958.1	5.37	.811	.6936	.4890	.2764	1.5691	.2777	.3782
B. <i>Loans to States and Local Government</i>									
B1 Slum Clearance	15.3	3.95	.597	.5000	12.0000	.0498	.4038	.0753	.0973
Total	19.4	3.12	.471	.4000	.8000	.0465	.3645	.0654	.0878
C. <i>Projects within States</i>									
C1 Forest Highways	18.9	.82	.124	.1000	.5000	.2143	7.0338	1.2308	1.6951
C2 Army Corps of Engineers—civil projects	533.2	.62	.094	.0800	.1175	.0240	1.0247	.1815	.2470
C3 Bonneville Power Admin.	47.7	All groups nil except 10 richest states.							
C4 Reclamation	181.8								
C5 National Park Maintenance	32.8	.52	.079	.0577	.0217	.0395	1.6898	.3036	.4072
C6 National Forest Maintenance	30.0	.85	.128	.1064	.1667	.0862	2.6645	.4643	.6421
C7 Forest Roads and Trails	28.5	.79	.119	.1111	.2381	.1429	2.7903	.4878	.6725
C8 Soil Conservation	71.2	2.12	.320	.2768	.2199	.0960	.7320	.1289	.1764
Total	944.1	.60	.091	.0769	.1258	.0345	1.7883	.3165	.4310

Programs (brief titles):

D. *Grants and Payments to Individuals and Groups*

I II III IV V VI VII VIII IX

# TAXES AND TREASURY DISBURSEMENTS 221

	I	II	III	IV	V	VI	VII	VIII	IX
<b>Programs (brief titles):</b>									
<b>D. Grants and Payments to Individuals and Groups</b>									
D1 V. A. Readjustment Benefits	574.2	5.09	.769	.6574	.4188	.2211	1.2735	.2256	.3069
D2 V. A. Vocational Rehabilitation	41.0	5.52	.834	.7188	.6216	.2201	1.2476	.2201	.3007
D3 V. A. pensions	2368.8	7.25	1.095	.9366	.6963	.3938	2.0377	.3606	.4911
D4 Railroad Retirement Board—various benefits	648.1	3.43	.518	.4430	.3417	.2318	2.5097	.4439	.6048
D5 Ag. Conservation program	171.8	1.59	.240	.2037	.1599	.0618	.7252	.1287	.1748
D6 Commodity Stabilization—sugar	37.9	N. E. = nil.			ESC = nil.		1.5353	.2677	.3700
D7 Ag.—disaster emergency funds	76.2	N. E. = nil.					.0431	.0068	.0104
D8 National Institutes of Health—fellowships, etc.	43.2	16.6	2.514	2.1471	2.2813	2.3175	4.7071	.8310	1.1344
D9 Bureau Lab. payments for veterans	78.1	5.22	.789	.6748	.3416	.1504	.8619	.1521	.2077
D10 Withdrawal payroll tax insurance fund	2015.1	7.68	1.160	.9924	1.0805	.6436	4.1905	.7416	1.0099
D11 Commodity Stabilization	36.2	.19	.029	.0175	.0076	.0036	.3142	.0551	.0757
D12 Maritime Administration	85.0	N. E., S. A., and ESC = nil.			.53476	.9444	1.2888		
D13 Old Age benefits	3633.0	9.11	1.377	1.1766	1.0996	.9393	4.4257	.7831	1.0666
Total	9824.5	7.39	1.117	.9554	.8315	.5297	2.9463	.5213	.7101
<b>E. Loans to Individual and Groups</b>									
E1 S. B. A. regular loans	26.9	3.16	.477	.4048	.3778	.1771	1.7238	.3053	.4154
E2 V. A. direct loans	117.7	1.57	.237	.2000	.0843	.0551	.6172	.1085	.1487
E3 Loans under FCA	2157.9	3.11	.470	.4021	.3803	.1825	1.0776	.1906	.2597
E4 Loans under Rural Electrification	235.7	.05	.008	.0081	.0051	.0018	.4144	.0736	.0999
E5 Loans under Farmers Home Administration	280.5	1.78	.269	.2290	.1772	.0924	.3948	.0699	.0951
E6 Loans under CCC (non-recourse)	3304.7	.06	.009	.0081	.0109	.0025	.6664	.1180	.1606
E7 Loans under CCC (storage facilities, etc.)	13.5	N. E. = nil.					.5386	.0938	.1298
E8 Housing loans for Ed. Inst.	34.9	N. E. = nil.					2.3860	.4250	.5750
Total	6173.3	1.26	0.190	.1621	.1707	.0568	.7738	.1369	.1865
<b>F. Loan Guaranties and Insurance</b>									
F1 V. A. Privatee loans	1855.5	9.31	1.407	1.2027	1.1897	1.1809	5.9382	1.0507	1.4311
F2 FHA—mortgages insured	3069.0	3.96	.598	.5119	.4884	.4204	5.3017	.9381	1.2777
Total	4934.0	5.97	.902	.7711	.7447	.6716	5.4783	.9604	1.3203
<b>G. Non Tax-Financed Insurance Payments</b>									
G1 V. A. Life insurance	408.8	6.64	1.003	.8583	.6422	.4043	2.2114	.3915	.5329
Total	408.8	6.64	1.003	.8583	.6422	.4043	2.2114	.3915	.5329

Programs (brief titles):													
H. <i>Salaries, Services and Procurement</i>													
I	II	III	IV	V	VI	VII	VIII	IX					
				N. E. = nil, E.S.C. = nil, 10 poorest states = nil.									
51.0 } 36.4 }	6.16	.931	.7959	.6419	.3555	2.0306	.3591	.4894					
H1 Advisory Comm. Aeronautics—supplies	891.9	8.43	1.274	1.0933	.7130	1.2615	3.1473	.5619					
H2 Advisory Comm. Aeronautics—salaries	48.0	2.04	.308	.2652	.5041	.0175	.0725	.7985					
H3 V. A. admin. expenses & salaries	146.6							.0992					
H4 V. A. hospital construction & facilities	117.1												
H5 TVA Procurement	37.3	.19	.029	.0169	.0054	.0217	.2468	.3296					
H6 TVA Salaries	17.1												
H7 Ag. Research Service—expenses & salaries	19.1	4.41	.666	.5667	.4595	.3864	1.5051	.2609					
H8 Ag. Pest Control—expenses & salaries	14.1	3.42	.517	.4545	.7692	.500	5.1541	.9286					
H9 Meat Control—expenses & salaries	30.0	.85	.128	.1064	.1667	.0862	2.6645	.4643					
H10 Forest Pest Control, etc.	67.7	7.55	1.141	.9811	1.3867	.3954	1.9639	.3482					
H11 Air National Guard	115.8	8.60	1.299	1.1099	.6711	.5037	1.5089	.2673					
H12 Public Health Service	86.9	2.25	.340	.2941	.0640	.2564	1.3436	.2379					
H13 Compensation of Postmasters	127.7	6.33	.956	.8159	.5109	.3260	1.2260	.2175					
H14 Post Office maintenance, etc.	97.4	7.17	1.083	.9281	.8161	.6698	3.8654	.6814					
H15 Mail deliveries, etc.	1619.3	6.94	1.049	.8962	.8726	.6768	4.2424	.7506					
H16 Ship construction	72.1	4.99	.754	.6460	.2098	.2296	4.6000	.8115					
H17 Bureau Old Age insurance, expenses & salaries	62.8	3.36	.508	.4343	.0984	.3028	3.5737	.6237					
Total	3663.5	5.84	.882	.7546	.5720	.2477	2.1864	.3869					
Total Expenditures	7799.1	6.36	.961	.8217	.6822	.3724	2.4014	.4249					
Total Loans Closed	6192.7	1.26	.190	.1630	.1718	.0567	.7719	.1366					
Total Loans Insured	4934.0	5.97	.902	.7711	.7447	.6716	5.4783	.9694					

Note: The 10 richest and 10 poorest states were selected from the 1953 tables of state income payments (*Survey of Current Business*, August 1954). The 1954 tables could not be used since they were not published until this study was well under way; in any case the difference would have been slight—a matter of one state.

The states used in our calculations are:

		10 Richest		10 Poorest	
California	Nevada	Alabama	Mississippi		
Connecticut	New Jersey	Arkansas	North Carolina		
Delaware	New York	Georgia	South Carolina		
Illinois	Ohio	Kentucky	Tennessee		
Michigan	Washington	Louisiana	West Virginia		

# TAXES AND TREASURY DISBURSEMENTS 223

Disbursements in New York per Thousand Dollars of Taxes  
as a Percentage of That in the United States  
(Programs costing more than \$25 million)

Program	%
A3 Public Housing Contribution	58.6
A5 Agricultural Extension Work	16.7
A7 Dept. of Agriculture school lunch program	38.2
A8 Dept. of Agriculture surplus commodities	42.0
A10 Aid Highways	36.3
A12 School districts grants	17.6
A13 School construction	15.3
A16 Hospital construction	25.0
A17 Old Age Assistance	29.3
A18 Dept. Health grants for disabled	138.8
A19 Dept. Health grants to blind	34.5
A20 Dept. Health aid to dependent children	71.0
A23 Payments from mineral leasing	N. Y. = nil
A25 Employment security grants	95.2
Total Aid to State and Local Government	43.9
C2 Army Corps of Engineers, civil projects	8.1
C3 Bonneville Power Administration	0.0
C4 Reclamation	0.0
C5 National Park maintenance	7.7
C6 National Forest maintenance	0.0
C7 Forest roads and trails	0.0
C8 Soil conservation	14.3
Total Projects within States	5.9
D1 VA Readjustment benefits	49.0
D2 VA vocational rehabilitation	45.3
D3 Pensions	58.5
D4 Railroad Retirement Board—various benefits	46.8
D5 Agricultural Conservation Program	14.1
D6 Commodity Stabilization—sugar	0.0
D7 Agricultural Disaster emergency funds	0.0
D8 National Institutes of Health, fellowships, etc.	104.4
D9 Bureau of Labor—payments to veterans	30.1
D10 Withdrawals payroll insurance fund	90.6
D11 Commodity stabilization	3.5
D12 Maritime Administration	411.2
D13 Old Age Benefits	77.6
Total Grants and Payments to Individuals and Groups	72.9
E1 SBA Regular loans	31.0
E2 VA Direct loans	8.1
E3 Loans under FCA	15.0
E4 Loans under REA	0.0
E5 Loans under Farmers Home Administration	7.7
E6 Loans under CCC (non-recourse)	2.6
E8 Housing loans for educational institutions	83.6
Total Loans to Individuals & Groups	7.8

Disbursements in New York per Thousand Dollars of Taxes  
as a Percentage of That in the United States (*Continued*)  
(Programs costing more than \$25 million)

Program		%
F1	VA Private loans	92.2
F2	FHA—mortgages insured	54.7
	Total Loan Guarantees & Insurance	68.7
G1	VA Life insurance	57.5
	Total Non-Tax Financed Insurance Payments	57.5
H1	Advisory Comm. Aeronautics—supplies	0.0
H2	Advisory Comm. Aeronautics—salaries	0.0
H3	VA administration expenses & salaries	57.0
H4	VA hospital construction & facilities	28.0
H5	TVA procurement	47.0
H6	Salaries	0.0
H7	Agricultural Research Service—expenses & salaries	5.1
H10	Forest pest control, etc.	0.0
H11	Air national guard	64.2
H12	Army national guard	46.7
H13	Public Health Service	60.3
H14	Compensation of postmasters	35.3
H15	Post Office maintenance, etc.	126.8
H16	Mail delivery, etc.	99.6
H17	Ship construction	0.0
H18	Bureau of Old Age Insurance—expenses & salaries	60.0
	Total Salaries, Services & Procurement	70.0
EX	Total Expenditures	63.2
LI	Total Loans Insured	68.7
LC	Total Loans Closed	9.8

Ten Richest and Ten Poorest States: Percentage of Former to Latter Relative  
Disbursements and in Relation to Taxes Borne and Income, 1954

Program	Amounts (\$ million)	Disbursements, 10 Richest		Disbursements, Relative to Taxes, 10 Richest		Disbursements, Relative to Income, 10 Richest	
		Disbursements, 10 Poorest		Ibid., 10 Poorest		Ibid., 10 Poorest	
Grants: Highways	532	168		30		41	
School Construction	104	154		27		37	
Old Age Assistance	957	159		28		38	
Permanently Disabled	74	148		26		36	
Dependent Children	360	160		28		39	
Employment Security	198	375		66		90	
Projects within States	944	178		32		43	
Grants and Payments to Individuals: V. A. Pensions	2,369	204		36		49	
Withdrawals: Employment Security	2,015	419		74		101	
Old Age and Survivors Insurance	3,633	443		78		107	
All Grants to Individuals and Groups	9,824	295		52		71	
Loans: Guarantees and Insurance							
V. A. Private	1,855	594		105		143	
FHA	3,069	530		94		128	
Salaries	3,664	219		39		53	
All Expenditures	17,799	240		42		58	
All Loans Closed	6,193	77		14		19	
Loans: Insured, etc.	4,934	548		97		132	

\* See Master Table for listing of these states.

Programs Costing More Than \$25 Million  
The Ratio of Disbursements in New England per Thousand  
Dollars of Taxes to That in the United States—  
1953 and 1954

$\left( \left[ \frac{\text{Disbursements}}{\$1,000 \text{ taxes}} \right] \text{ N. E.} + \left[ \frac{\text{Disbursements}}{\$1,000 \text{ taxes}} \right] \text{ U. S.} \right)$			
Program	1953	1954	
A3 Public Housing contribution	(1.4194)	1.3793	
A5 Agricultural Extension work	.4167	.4167	
A7 Dept. Agriculture, school lunch program	.5968	.6016	
A8 Dept. Agriculture, surplus commodities	.6765	.9076	
A10 Aid highways	.6451	.6168	
A12 School districts grants	.5657	.6471	
A13 School construction	.2951	.1288	
A16 Hospital construction	.4970	.4848	
A17 Old Age assistance	.8062	.7527	
A18 Dept. Health, grants for disabled	.7283	.8966	
A19 Dept. Health, grants to blind	.4902	.5000	
A20 Dept. Health, aid dependent children	.6705	.6431	
A23 Payments from mineral leasing	N. E. = 0	N. E. = 0	
A25 Employment security grants	1.0682	1.0257	
Total Aid to State and Local Government	.7046	.6936	
C2 Army Corps of Engineers, civil projects	.0813	.0800	
C3 Bonneville Power Administration	N. E. = 0	N. E. = 0	
C4 Reclamation	N. E. = 0	N. E. = 0	
C5 National Park maintenance	.1224	.0577	
C6 National Forest maintenance	.1042	.1064	
C7 Forest roads and trails	.1471	.1111	
C8 Soil conservation	.2870	.2768	
Total Projects within States	.0770	.0769	
D1 V. A. readjustment benefits	.5928	.6574	
D2 V. A. vocational rehabilitation	.6444	.7188	
D3 V. A. pensions	.9388	.9366	
D4 Railroad Retirement Board, various benefits	.4609	.4430	
D5 Agricultural Conservation Program	.2391	.2037	
D6 Commodity Stabilization—sugar	N. E. = 0	N. E. = 0	
D7 Agriculture Disaster Emergency funds	N. E. = 0	N. E. = 0	
D8 National Institutes of Health fellowships, etc.	2.000	2.1471	
D9 Dept. of Labor, payments to veterans	(.8919)	.6748	
D10 Withdrawals payroll insurance fund	1.0107	.9924	
D11 Commodity Stabilization	.1176	.0175	
D12 Maritime Administration	N. E. = 0	N. E. = 0	
D13 Old Age benefits	1.1964	1.1766	
Total Grants and Payments to Individuals and Groups	.9502	.9554	



# TAXES AND TREASURY DISBURSEMENTS 227

Programs Costing More Than \$25 Million  
The Ratio of Disbursements in New England per Thousand  
Dollars of Taxes to That in the United States—  
1953 and 1954 (*Continued*)

$\left( \left[ \frac{\text{Disbursements}}{\$1,000 \text{ taxes}} \right] \text{N. E.} + \left[ \frac{\text{Disbursements}}{\$1,000 \text{ taxes}} \right] \text{U. S.} \right)$			
Program	1953	1954	
E1 S. B. A. regular loans	nil	.4048	
E2 V. A. direct loans	.1912	.2000	
E3 Loans under FCA	.4609	.4021	
E4 Loans under REA	.1905	.0081	
E5 Loans under Farmers Home Administration	.2101	.2290	
E6 Loans under CCC (non-recourse)	.2149	.0081	
E8 Housing loans for educational institutions	1.000	N. E. = 0	
Total Loans to Individuals and Groups	.2747	.1621	
F1 V. A. private loans	1.1530	1.2027	
F2 FHA mortgages insured	.4892	.5119	
Total Loan Guaranties and Insurance	.7239	.7711	
G1 V. A. life insurance	.8600	.8583	
Total Non-Tax Financed Insurance Payments	.8600	.8583	
H1 Advisory Commission Aeronautics, supplies	N. E. = 0	N. E. = 0	
H2 Advisory Commission Aeronautics, salaries	N. E. = 0	N. E. = 0	
H3 V. A. administrative expenses and salaries	.7539	.7959	
H4 V. A. hospital construction and facilities	2.1905	1.0933	
H5 TVA procurement	.4410	.2652	
H6 TVA salaries	N. E. = 0	N. E. = 0	
H7 Agricultural Research Service, expenses and salaries	.0426	.0169	
H10 Forest pest control, etc.	(.2381)	.1064	
H11 Air National Guard	1.1333	.9811	
H12 Army National Guard	1.1366	1.1099	
H13 Public Health Service	.3525	.2941	
H14 Compensation of postmasters	.8069	.8159	
H15 Post Office maintenance, etc.	1.3395	.9281	
H16 Mail delivery, etc.	.9053	.8962	
H17 Ship construction	2.1381	.6460	
H18 Bureau Old Age Insurance, expenses and salaries	(.4330)	.4343	
Total Salaries, Services and Procurement	.8465	.7546	
EX Total Expenditures	.8204	.8217	
LC Total Loans Closed	.2751	.1630	
LI Total Loans Insured	.7240	.7711	

Note: Figures in parentheses indicate that programs cost less than \$25 million in 1953 but more in 1954.

Programs Costing More Than \$10 Million, 1954  
Full Titles of Programs in Master Table

(Source of original figures on disbursements is given in parentheses after each item)

A Grants to States and Local Units

- A1 Federal Civil Defense Administration, Federal contributions to the states (*Annual Report of the Secretary of the Treasury on the State of the Finances*, hereafter cited as *Finances*).
- A2 Housing and Home Finance Agency, Office of the Administrator, grants for slum clearance and urban redevelopment (*Finances*).
- A3 Housing and Home Finance Agency, Public Housing Administration, annual contribution to state and local authorities (*Finances*).
- A4 Department of Agriculture, Agricultural Research Service, payments to states for experiment stations (*Finances*).
- A5 Department of Agriculture, Agricultural Extension Service, cooperative extension work (*Finances*).
- A6 Department of Agriculture, Forest Service, National Forest Funds, shared revenues (*Finances*); includes payments to school funds, Arizona and New Mexico.
- A7 Department of Agriculture, Agricultural Marketing Service, national school lunch program (*Finances*); includes value of commodities distributed but excludes those donated by the Commodity Credit Corporation.
- A8 Department of Agriculture, Agricultural Marketing Service, removal of surplus agricultural commodities (*Finances*); value of commodities distributed at cost to Commodity Credit Corporation.
- A9 Department of Commerce, Civil Aeronautics Administration, grants to states under the Federal Airport Act (*Finances*).
- A10 Department of Commerce, Bureau of Public Roads, Federal aid highways (*Finances*); includes access roads, elimination of grade crossings, public land highways and other programs.
- A11 Department of Health, Education and Welfare, Office of Education, grants for vocational education (*Finances*).
- A12 Department of Health, Education and Welfare, Office of Education, payments to school districts for maintenance and operation of schools (*Finances*).
- A13 Department of Health, Education and Welfare, Office of Education, grants for school construction (*Finances*); does not include payments to Housing and Home Finance Agency for construction of Federally owned schools.
- A14 Department of Health, Education and Welfare, Office of Vocational Rehabilitation, grants to states (*Finances*).
- A15 Department of Health, Education and Welfare, Public Health Service, grants under various disease control and general health assistance programs (*Finances*); includes supplies furnished to states.
- A16 Department of Health, Education and Welfare, Public Health Service, grants for hospital construction (*Finances*).
- A17 Department of Health, Education and Welfare, Social Security Administration, Bureau of Public Assistance, grants for old age assistance (*Finances*).
- A18 Department of Health, Education and Welfare, Social Security Administration, Bureau of Public Assistance, grants for aid to the permanently disabled (*Finances*).
- A19 Department of Health, Education and Welfare, Social Security Administration, Bureau of Public Assistance, grants for aid to the blind (*Finances*).
- A20 Department of Health, Education and Welfare, Social Security Administration, Bureau of Public Assistance, grants for aid to dependent children (*Finances*).
- A21 Department of Health, Education and Welfare, Social Security Administration, Children's Bureau, grants for maternal and child health services (*Finances*).

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- A22 Department of Health, Education and Welfare, Social Security Administration, Children's Bureau, grants for services for crippled children (*Finances*).
  - A23 Department of the Interior, Bureau of Land Management, payments out of receipts under the Mineral Leasing Act and from special funds (*Finances*); includes payments to states from grazing receipts, to Oklahoma from gas and oil royalties, to counties in California and Oregon in lieu of taxes on land grants and to Arizona and Nevada from the Colorado River Dam Fund.
  - A24 Department of the Interior, Fish and Wildlife Service, grants to states (*Finances*); comprises Federal aid for wildlife and fish restoration and payments under the Migratory Bird Conservation Act.
  - A25 Department of Labor, Bureau of Employment Security, grants to states (*Finances*); this item may involve duplication of part of the amount listed under D10 which covers total withdrawals from the payroll tax trust fund administered by the BES.
- B    *Loans to States and Local Authorities (Gross)*
- B1 Housing and Home Finance Agency, Office of the Administrator, loans to states for slum clearance and urban redevelopment (supplied upon request to agency).
- C    *Projects within States*
- C1 Department of Commerce, Bureau of Public Roads, forest highways (*Finances*).
  - C2 Department of Defense, Army Corps of Engineers, civil projects (supplied upon request to agency).
  - C3 Department of the Interior, Bonneville Power Administration, total expenses (supplied upon request to agency); estimated allocation by BPA based upon distribution of fixed investment.
  - C4 Department of the Interior, Bureau of Reclamation, total expenditures on reclamation projects (supplied upon request to agency); expenditures on multi-state projects divided evenly among states involved.
  - C5 Department of the Interior, National Park Service, total expenditures for park maintenance and development (supplied upon request to agency); obligations distributed by location of park.
  - C6 Department of Agriculture, Forest Service, national forest protection and maintenance (*Department of Agriculture, Project Breakdown*, hereafter cited as *Projects*).
  - C7 Department of Agriculture, Forest Service, forest roads and trails (*Projects*).
  - C8 Department of Agriculture, Soil Conservation Service, operating expenses (*Projects*); includes flood prevention, soil conservation, watershed protection and technical aid to farmers.
- D    *Grants and Payments to Individuals and Groups*
- D1 Veterans Administration, readjustment benefits under Public Laws 364 and 550 (*Annual Report of the Administrator of Veterans Affairs*, hereafter cited as *Veterans*).
  - D2 Veterans Administration, vocational rehabilitation under Public Laws 16 and 894 (*Veterans*).
  - D3 Veterans Administration, pensions (*Veterans*).
  - D4 Railroad Retirement Board, unemployment, temporary disability, retirement and death benefits (*Annual Report of the Railroad Retirement Board*).
  - D5 Department of Agriculture, Agricultural Conservation Program Service, payments to farmers (*Finances*).
  - D6 Department of Agriculture, Commodity Stabilization Service, administration of the Sugar Act Program (*Finances*).
  - D7 Department of Agriculture, Commodity Credit Corporation, Disaster Emergency funds (*Finances*).

- D8 Department of Health, Education and Welfare, Public Health Service, National Institutes of Health, fellowships, research grants and trainee awards (*Finances*).
- D9 Department of Labor, Bureau of Employment Security, payments to veterans (*Finances*).
- D10 Department of Labor, Bureau of Employment Security, withdrawals by states from the payroll tax trust fund on account of benefits payable (supplied upon request to agency); calendar year; may include item A25.
- D11 Department of Agriculture, Commodity Stabilization Service, agricultural adjustment programs (supplied upon request to agency); exclusive of payments under the Sugar Act and loans provided by the Commodity Credit Corporation.
- D12 Department of Commerce, Maritime Administration, operating differential subsidy (supplied upon request to agency); by location of business office of steamship company receiving subsidy payments.
- D13 Department of Health, Education and Welfare, Social Security Administration, Bureau of Old Age and Survivors Insurance, benefits paid (supplied upon request to agency); calendar year.

E *Loans to Individuals and Groups (Gross)*

- E1 Small Business Administration, regular loans (*Annual Report of the Small Business Administration*); period from August 1, 1953 to July 31, 1954.
- E2 Veterans Administration, direct loans to veterans (*Veterans*); gross value issued as difference between cumulative totals for 1953 and 1954, by office of issue; residents of Connecticut, Delaware, the District of Columbia, Massachusetts, New Hampshire, New Jersey, Rhode Island, New York City and Philadelphia ineligible for these loans.
- E3 Farm Credit Administration, gross value of loans closed by agencies under supervision of the F.C.A. (supplied upon request to agency); includes loans closed by the Federal Land Banks, the Federal Intermediate Credit Banks, the Production Credit Associations and the Banks for Cooperatives; excludes Federal Intermediate Credit Bank loans to the Production Credit Associations and Banks for Cooperatives; note that these loans are financed out of funds raised by the sale of bonds to the public without Federal guarantee.
- E4 Department of Agriculture, Rural Electrification Administration, net value of loans (*Projects*).
- E5 Department of Agriculture, Farmers Home Administration, direct loans (supplied upon request to agency); includes water, production, orchard, farm ownership and farm housing loans.
- E6 Department of Agriculture, Commodity Credit Corporation, non-recourse loans (*Statement of Operations and Financial Condition of the Commodity Credit Corporation*); on 1952 crops through the end of fiscal 1953 and on 1953 crops through the end of fiscal 1954.
- E7 Department of Agriculture, Commodity Credit Corporation, storage facilities and equipment loans (supplied upon request to agency).
- E8 Housing and Home Finance Agency, Office of the Administrator, housing loans to educational institutions (supplied upon request to agency); includes loans to public educational institutions totalling about 40 per cent of the listed amount.

F *Value of Loan Guaranties and Insurance (Gross)*

- F1 Veterans Administration, guaranties of private loans to veterans (*Veterans*); gross value issued as difference between cumulative totals for 1953 and 1954, by office of issue.
- F2 Housing and Home Finance Agency, Federal Housing Administration, mortgages insured (supplied upon request to agency); by location of property and by calendar year.

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### G *Non-Tax Financed Insurance Payments*

- G1 Veterans Administration, life insurance payments, all programs (*Veterans*).

### H *Salaries, Services and Procurement*

- H1 National Advisory Commission for Aeronautics, supplies and services purchased (supplied upon request to agency); allocation by location of disbursing unit.
- H2 National Advisory Commission for Aeronautics, salaries (supplied upon request to agency); allocation by location of disbursing unit.
- H3 Veterans Administration, administrative expenses including salaries (*Veterans*); may include some benefit payments of the type ordinarily classified under title D; excludes disbursements from supply fund.
- H4 Veterans Administration, construction and related costs of hospital and domiciliary facilities (*Veterans*).
- H5 Tennessee Valley Authority, procurement (supplied upon request to agency); by point of manufacture or processing.
- H6 Tennessee Valley Authority, salaries (supplied upon request to agency); by site at which services were rendered.
- H7 Department of Agriculture, Agricultural Research Service, research expenses (including salaries) (*Projects*).
- H8 Department of Agriculture, Agricultural Research Service, plant disease and pest control, operating expenses including salaries (*Projects*).
- H9 Department of Agriculture, Agricultural Research Service, meat inspection, operating expenses including salaries (*Projects*).
- H10 Department of Agriculture, Forest Service, pest control and brush disposal, operating expenses including salaries (*Projects*).
- H11 Department of Defense, Air National Guard, payments to state agencies administering program (*Finances*).
- H12 Department of Defense, Army National Guard, payments to state agencies administering program (*Finances*).
- H13 Department of Health, Education and Welfare, Public Health Service, operating expenses including salaries (supplied upon request to agency); by location of regional office.
- H14 Post Office Department, compensation of postmasters (supplied upon request to agency).
- H15 Post Office Department, rental, maintenance of buildings, utilities and services (supplied upon request to agency).
- H16 Post Office Department, mail delivery and collection, clerical and contractual services including salaries (supplied upon request to agency).
- H17 Department of Commerce, Maritime Administration, ship construction and repair (supplied upon request to agency); by location of shipyard.
- H18 Department of Health, Education and Welfare, Social Security Administration, Bureau of Old Age and Survivors Insurance, operating expenses including salaries (supplied upon request to agency); estimated on the basis of workload and regional distribution of benefits.

## MONETARY POLICY IN UNDERDEVELOPED COUNTRIES

*Arthur I. Bloomfield\**

### INTRODUCTION

**I**N the underdeveloped countries of the world, although to a considerably lesser extent than in the developed ones, there has in recent years been a growing interest in and resort to monetary policy as an instrument of economic control. In particular, there has been a lively interest in the underdeveloped countries in the potentialities of monetary policy as a means of promoting the objective of more rapid economic development.

To some degree this interest reflects a greater awareness than before of the fact that, as the prospect for massive foreign and international grants and loans recedes, economic development must depend increasingly on enlarging, mobilizing and channeling *domestic* real resources; monetary as well as fiscal policy have consequently assumed increased importance. There has likewise been a growing appreciation of the importance of monetary stability as a prerequisite for sound and balanced development. But in substantial part also this interest stems from the fact that in recent years a large number of underdeveloped countries have established central banks, or have reorganized pre-existing ones, with the result that many underdeveloped countries are now able for the first time to pursue a monetary policy of their own or have more adequate powers than before to make their monetary policy felt. Since 1945 central banks have been newly established or thoroughly reorganized in no less than some 27 underdeveloped countries

\* This paper represents a somewhat revised version of a talk delivered before a combined meeting of the International Economics Seminar and the Fiscal Policy Seminar of the Graduate School of Public Administration at Harvard University on April 22, 1955. Its conclusions have been shaped in part by the writer's experiences in the Far East, where he advised on the establishment of a number of central banks.

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or areas.<sup>1</sup> In other cases, moreover, the powers of existing central banks have been somewhat broadened.

Where central banks were newly set up, a variety of methods were used. Some of these methods included: taking over and enlarging the functions of a pre-existing Currency Board (e.g., Ceylon and Iraq) or a note-issuing agency of the Treasury (e.g., the Philippines); separating out, and enlarging the scope of, the issue department of a pre-existing bank of issue engaging also in a commercial banking business (e.g., Israel, Guatemala, Costa Rica, and Indonesia); or splitting up a pre-existing central bank serving several geographical areas into separate national central banks (e.g., South Vietnam, Cambodia, Laos, and Pakistan). Central banks were also set up in a few countries where previously only foreign currency notes had circulated (e.g., the Dominican Republic), or where local currency notes had previously been issued by private commercial banks (e.g., Honduras).

Like most central banks everywhere, the great majority of central banks in underdeveloped countries, and nearly all those established or reorganized in recent years, are fully owned by the government. Even when not fully owned, they are usually partially owned, by the government. The government generally appoints a majority or all of the members of the managing boards, including the chief executive officers; and government officials, usually including the Minister of Finance, are often themselves board members. Nevertheless, various administrative provisions are inserted in many of the statutes with the object of trying to secure for the central bank the largest possible measure of independence from political direction and pressures, and of freedom in formulating and implementing monetary policy, while fostering the maximum of coordination

<sup>1</sup> The countries or areas concerned are: Belgian Congo, Burma, Cambodia, Ceylon, Chile, Costa Rica, Cuba, the Dominican Republic, Ecuador, Egypt, French Equatorial Africa and the Cameroons, French West Africa and Togo, Guatemala, Honduras, Indonesia, Iraq, Israel, Laos, Libya, Pakistan, Paraguay, the Philippines, Rhodesia and Nyasaland, South Korea, South Vietnam, Nepal and Syria. In a number of these cases, the establishment of central banks was closely associated with the achievement of political independence by the countries concerned.

We see no need to elaborate here upon the definition of an underdeveloped country. For purposes of this paper, we shall include the countries of Latin America, the Middle East, Africa (except the Union of South Africa), and Asia and the Far East (except Australia, New Zealand and Russia).



between government and central bank policies. Many of the statutes, moreover, contain provisions strictly limiting the amount of loans and advances that the central bank may make to the government, and some of them also limit the amount of government securities that the central bank may take up, directly or indirectly. Legal provisions, however, are of course no guarantee against undue government interference in central bank affairs or against excessive government recourse to central bank credit—as the experience of many countries has amply demonstrated.

Many of the new central banks, especially those established with the help of Federal Reserve advisers, are characterized by unusually wide and flexible powers designed to promote internal and external stability and economic development. A large number of instruments of general and selective credit control, some of a novel character, and some involving a broad measure of direct control over bank portfolios, are provided for. Powers are given to the central bank to engage in an unusually wide range of credit operations with the commercial banks and in some cases with other financial institutions or with the public itself. Broad responsibility is delegated to the central bank to manage the country's international reserves. These and other powers were specifically provided for in the hope of enabling the central banks concerned to pursue a more purposive and effective monetary policy than had been possible for most of the central banks that had been set up in underdeveloped countries during the twenties and thirties. Those banks had been equipped with exceedingly orthodox statutes and limited powers which permitted little flexibility or scope for monetary policy and which were sometimes poorly adapted to the primitive financial structures of the countries concerned.

This paper has the objective of broadly surveying the role and problems of monetary policy in underdeveloped countries in general, reviewing some of the lessons of recent experience, and outlining some of the measures that the central bank might take to promote economic development with stability and to enhance the effectiveness of its policies in the future.<sup>2</sup>

<sup>2</sup> Rather than clutter up the text with bibliographical citations, a list of selected writings on the monetary and banking problems of underdeveloped countries is appended at the end of this article.

To keep the paper within manageable limits, although admittedly at the cost of some narrowing of its scope, only incidental attention will be paid to foreign exchange and payments policies. Such policies, which are almost invariably a direct responsibility of the government but are usually administered by the central bank, are of course really part of monetary policy proper. Likewise, relatively little will be said about fiscal and debt management policies and the administration of Treasury cash balances, although these may have an effect on the course of monetary events at times far exceeding that exerted by central bank policy alone. The focus, therefore, will be predominantly on central bank policies designed to influence the supply, availability and cost of loanable funds in the economy generally and their distribution as between different sectors of the economy. Admittedly, such a separation of central bank policies and government financial policies is somewhat artificial in view of the need for close coordination between the two, especially in underdeveloped countries where the public sector is often unusually large.

Nor will this paper concern itself, except incidentally, with the monetary problems of those underdeveloped countries that do not as yet have genuine central banks, since in such cases there is usually little if any scope for monetary policy. These countries are mainly dependent territories, largely in Africa, that are serviced by Currency Boards or their equivalents which operate for the most part on the basis of automatic 100 per cent exchange reserve systems.<sup>3</sup>

Generalizations about underdeveloped countries, whether on monetary policy or on more important matters, are likely to be especially hazardous. Despite the many broad similarities which these countries exhibit, there are often substantial differences in resource endowment, in population densities, in the degree of dependence upon foreign trade, in the strength of development drives, in exchange and payments systems, in the extent of development of financial structures, in political and socio-cultural frameworks and in other respects. It is believed,

<sup>3</sup> Reference might also be made to one or two countries, notably Brazil, where central banking functions are divided between a banking institution, which is not a full-fledged central bank, and the government or its agencies. Such countries, however, fall within the scope of this article.

however, that the generalizations made in this paper are valid for the great majority of underdeveloped countries.

#### THE INSTITUTIONAL SETTING OF MONETARY POLICY IN UNDERDEVELOPED COUNTRIES

Among the many institutional characteristics common to underdeveloped countries in general are some of special relevance in influencing the potential role, scope, and effectiveness of monetary policy.

Money does not play the same pervasive role that it does in economically advanced countries. A substantial portion of the agricultural production, which bulks so large in the aggregate output of most underdeveloped countries, is usually of a subsistence rather than market character. In many rural areas in these countries, moreover, barter transactions rather than purchase and sale predominate, money being used mainly for the payment of taxes or for the purchase of a narrow range of essential goods from the market sector of the economy. A considerable part of the aggregate economic activity of underdeveloped countries is thus often outside the scope of monetary policy.

As is well known, externally-generated fluctuations play an especially important role in the economic life of the majority of underdeveloped countries in view of their heavy dependence upon exports. Since their exports consist mainly of primary products subject to wide swings in world demand and prices, underdeveloped countries tend to undergo wide externally-generated swings in their external reserves, money supply and money incomes. The primary changes in the money supply associated with such swings are not easily subject to the direct control of the central bank nor, as will be noted, can they easily be offset by central bank action on that part of the money supply which is so subject.

Changes in the volume of central bank credit to the government and its agencies are often another important cause of changes in the money supply in underdeveloped countries because of strong development drives, inadequate tax systems and narrow markets in government securities. The central bank may have great difficulty in controlling such credit if

the government is insistent upon undue recourse to the central bank to finance its expenditures.

It is mainly, therefore, on that segment of the money supply which is generated by the commercial banks' credit operations with the private sector of the economy<sup>4</sup>—which is usually a relatively small segment of the money supply in most underdeveloped countries—that the central bank is able to exert its most direct influence. Thus, if the money supply tends to rise unduly because of large externally-induced acquisitions of exchange reserves or large central bank-financed budget deficits, it would probably be too much to expect the central bank to be able to *contract* commercial bank credit to the private sector, which will in fact be increasing its demands for accommodation<sup>5</sup> at a time when the commercial banks have a larger amount of reserves with which to lend. At best, the central bank may be able to do no more than prevent the commercial banks from adding further to the money supply on the basis of these added reserves, i.e., prevent a secondary expansion of the money supply. However, when an inflationary expansion of the money supply originates from an undue increase in commercial bank credit to the private sector, the central bank should be able to keep such expansion in check.

Difficulties would similarly tend to occur when there is an externally-induced decline in exchange reserves, the money supply and money incomes because of a drop in world demand for the country's exports. The central bank may be able at best to prevent the commercial banks from bringing about a secondary contraction in the money supply and additional deflationary pressures. If it *were* successful at such a time in inducing some credit expansion to the private sector, the drain on exchange reserves would tend to be increased, especially in the light of the high marginal propensity to import characteris-

<sup>4</sup> And by the central bank's credit operations with the private sector in those cases where the central bank engages in a commercial banking business. A distinction should be drawn between the foreign-trade and the domestic components of the private sector. Commercial bank credit usually goes mainly to the former.

<sup>5</sup> To take but one obvious example: a rising export surplus resulting from increased foreign demand and prices leads to larger demands upon the banks for credits to finance the larger aggregate value of foreign trade. In addition, the expansion in domestic activity, money incomes and money supply associated with a rising export surplus or a central bank-financed budget deficit stimulates increased demands from the private sector for bank credit in general.

tic of most underdeveloped countries. How far such counter-cyclical action could be pursued by the central bank, and in fact by the government, would thus depend upon the amount of exchange reserves that had previously been accumulated and upon whether or not and how far imports and other payments abroad were officially restricted.

In most underdeveloped countries, the banking habit is not as yet widespread. Banking touches only a relatively small part of the population. The use of checking accounts and other banking services is confined primarily to traders, businessmen and government entities. Savings accounts, however, are somewhat more widely used by the general public. Some 50 per cent or more of the money supply (as conventionally defined) usually takes the form of currency in circulation. One consequence of this high degree of preference for currency is to keep down the deposit-creating capacity of the commercial banks on the basis of any given accretion of reserves, since any given increase in bank loans and investments leads to a significant drain of currency into circulation, thereby depleting bank reserves and tending to reduce the ability of the banks further to expand their credit operations.<sup>8</sup> This may be a factor of some help to the monetary authorities on occasions when bank reserves are changing rapidly and cannot easily be controlled.

Underdeveloped countries are also characterized by the limited scope or virtual absence of money markets and especially of capital markets. There are few organized markets in bills or commercial paper. There is often a lack of discountable paper, commercial bank loans being commonly made on an over-draft basis. The markets in short- and long-term government securities are usually very narrow, as are the markets in corporate stocks. These factors limit the scope and effectiveness of central bank open-market operations and to some extent discount operations as well.

A major limitation on the growth of a capital market in underdeveloped countries lies in the low rate of personal and business saving in absolute terms and relative to national in-

<sup>8</sup> The degree of multiple deposit creation is likely to be further held down by the relatively high marginal propensity to import, which tends to result in substantial external drains on bank reserves when bank credit is expanded.

come. Besides, those who do save to any significant degree—mainly people in the upper income brackets and large business enterprises—usually prefer, especially at times of inflation, to invest the bulk of these savings themselves in forms that remain directly under their control—e.g., in inventories, real estate, and foreign exchange or in their own business—rather than to transfer these savings to others through purchases of government or corporate securities or through savings banks, insurance companies or other institutional investors.<sup>7</sup> This reluctance to transfer savings to others reflects the greater profitability or prestige value of investing directly in the forms mentioned above, fear of inflation which makes it desirable to invest in these forms, traditional habits, some lack of confidence in governments, corporations and institutional investors and in the liquidity of transferred savings, and in some cases political insecurity.

As a result of these various factors, the development of the capital market has been inhibited. Governments have to go all too often to the central bank for assistance in financing deficits. The private securities market has been hampered. (Corporate stock tends to be held closely by small family groups who do not in any case want control to pass out of their hands.) Institutional investors, such as savings banks and insurance companies, generally do not as yet play a significant role in the financial structure of underdeveloped countries, although in some countries of Latin America these and related collective savings institutions, such as social security funds, capitalization companies and mortgage institutions, have made considerable headway in recent years. Commercial banks, as will be noted below, engage to only a very limited degree or not at all in long-term lending. More and more, governments have had to turn to the establishment of development banks and other specialized financing institutions, operating in large part with public funds, as instruments for providing medium- and long-term loan funds and equity capital to industry and agriculture.

<sup>7</sup> Moreover, institutional investors themselves tend to put an unduly large part of the savings at their disposal into real estate or semi-speculative ventures. It should also be noted that where foreign-owned business enterprises are important in a country's economy, a large part of aggregate business saving tends to be transferred abroad rather than invested locally.



It follows from the underdeveloped nature of the money and capital markets that the interest rate structure in underdeveloped countries is largely unintegrated and that over a large part of the economy interest rates are relatively insensitive to the actions of the monetary authorities. Even within given sectors or localities of the market there is often a wide diversity of interest rates because of wide differences in the type and quality of risk or because of the forces of custom and tradition. There is an especially wide gap between interest rates in the so-called organized and unorganized sectors of the money market. Interest rates undeniably play a lesser role than they do in more developed countries in influencing the volume and direction of investment. In the *modus operandi* of monetary policy, the availability of credit factor is likely to be more important, relative to the cost factor, than it is in more developed countries. (In some cases, in fact, the authorities fix maximum loan rates for banks or official lending institutions.)

In most underdeveloped countries there is a marked lack of balance in the allocation of commercial bank credit. Commercial banks, in large part because of their traditional concern for a very high degree of liquidity, tend to concentrate heavily on short-term loans to finance foreign trade, domestic commerce, inventory holdings and related short-term transactions. Such loans are also likely to be more profitable than other types of lending. Loans for productive purposes to industry and agriculture, and especially medium- and long-term loans, usually constitute only a relatively negligible part of bank portfolios. Commercial banking facilities are concentrated mainly in urban centers. Established concerns tend to be favored over new ones, and large concerns over small ones. Branches of foreign banks, which play so important a role in the banking structure of underdeveloped countries, focus predominantly on servicing the foreign-trade sector of the economy.

Because of these banking habits and of a lack of "credit-worthiness," large sections of the population, especially farmers and small businessmen, cannot satisfy their credit needs through normal banking channels and must rely in large part upon moneylenders, merchants, and landowners at exorbitant interest rates. While such lenders cannot, to be sure, "create"



money, they can affect the income-velocity of money by influencing its rate of turnover and by providing money-substitutes, e.g., open-book credits; to some degree they can thus influence the aggregate volume of spending and the level of economic activity. Yet for the most part they are outside the reach of the monetary authorities.

Commercial banks in most underdeveloped countries tend to maintain the ratios of their reserves to deposit liabilities well in excess of the legal minima, where such are imposed. A substantial fraction of any increment of reserves, over and above that needed for legal requirements, tends to be held idle. This is another factor, along with the large internal and external drains noted earlier, tending to keep down the coefficient of multiple credit expansion. This tendency to maintain relatively large excess reserves reflects such factors as the lack of an adequate supply of short-term liquid assets that would provide suitable secondary reserves, the volatility of externally dependent underdeveloped countries, the susceptibility of the banks to large and sudden withdrawals of currency and the absence in many cases of a long-standing tradition of discounting at or borrowing from the central bank.

Since commercial banks in the majority of underdeveloped countries do not discount at or borrow from the central bank to any great extent or on a frequent or regular basis,<sup>8</sup> the potential effectiveness of the discount mechanism as a credit-control instrument in such countries is weakened. Since, moreover, the commercial banks tend to permit their holdings of excess reserves to undergo substantial fluctuations, the exact degree of their response to any given change in their reserves tends to be less predictable than in the more developed countries where banks usually keep relatively small excess reserves. Further limitations are thus imposed on the effective use of the traditional instruments of credit control.

Although all too little is known about the behavior of money in underdeveloped countries, there is reason to believe that the income-velocity of money in such countries tends, in the short run at least, to be much more stable than in developed ones. This stems from the fact that holdings of inactive money bal-

<sup>8</sup> There are, however, some notable exceptions to this rule, such as Japan, South Korea, Chile, Colombia, Paraguay, Guatemala, Costa Rica and Nicaragua.

ances tend to be relatively small (although in some Far Eastern countries a substantial amount of currency may be hoarded), or at least are not subject to large or sudden short-run shifts.<sup>9</sup> If the income-velocity of money does change significantly in the short run, it is generally because of changes in the rate of turnover of transactions balances, e.g., due to expectations of sharply rising or falling prices. Increases in the money supply (after allowance for the resulting drain through imports) thus tend ordinarily to be more closely correlated with increases in national money income in underdeveloped than in developed countries; additions to the money supply tend quickly to be spent on consumption or to provide the finance for investment, thereby raising incomes, and usually prices, until the added money is absorbed in larger transactions and finance balances. To the extent that the authorities have a firm control over the supply of money, this relative short-run stability of velocity would clearly be a factor working in favor of the effectiveness of monetary policy. But, for reasons already suggested, such control is often especially difficult to attain in underdeveloped countries.

The role and scope of monetary policy in underdeveloped countries are greatly influenced by the strong development drives to which most of them are subject. These drives, superimposed upon economies of low savings propensities, low taxable capacities and relatively inelastic outputs, make these countries highly sensitive to inflationary pressures and call for constant vigilance by the monetary authorities. They contribute to strong political pressures upon the central bank to extend credit unduly. They often make it necessary for the central bank to be more concerned with the development process, and to engage in a wider range of activities and operations, than is traditional with central banks in the more developed countries.

It is evident from the foregoing discussion that monetary policy faces special problems and limitations in underdeveloped countries which lie deep in the institutional structures of such

<sup>9</sup> It would be interesting to see how those who emphasize the "speculative motive" or "liquidity-preference proper" as "the" determinant of interest rates, with other demands for money being regarded as inelastic, would apply their doctrine to underdeveloped countries. We suspect that some substantial modifications would be necessary.

countries. It follows also that monetary policy in underdeveloped countries should not necessarily be evaluated in terms of the same standards and criteria applied in the more developed ones. The methods of implementing monetary policy, and the range and scope of central bank action, may well have to differ.

#### OBJECTIVES AND PRINCIPLES OF MONETARY POLICY IN UNDERDEVELOPED COUNTRIES

Fundamentally, the basic objectives of monetary policy, and indeed of fiscal policy, do not differ greatly in underdeveloped countries from those in more developed ones, despite the widely differing economic and social frameworks. Internal financial stability, high and rising levels of per capita income, and external payments balance: these are the major goals sought in each case.<sup>10</sup> But there is likely to be a very substantial difference in emphasis on these goals in the two sets of countries. In developed countries, the avoidance of inflation and deflation is usually the primary objective. In underdeveloped countries, on the other hand, the promotion of economic growth tends to overshadow all other goals of national economic policy; all too frequently, in fact, internal and external stability have been sacrificed in an attempt to achieve this basic objective.

A relatively large fraction of the saving that takes place in underdeveloped countries tends, as has been noted, to be diverted into investment expenditures of a sort that do not directly serve the ends of balanced economic development. The small upper-income group that provides the bulk of personal saving, moreover, usually engages in an inordinate amount of luxury consumption. If the current saving of this group were better mobilized, and if its lavish consumption outlays were kept in check, a significant amount of real resources could thereby be made available to the authorities for essential development expenditures. Additional resources for development could also be obtained by mobilizing a larger part of the retained profits of business enterprises which often find their way into relatively unessential uses from the viewpoint of balanced development. There is also scope in some cases for increasing the current savings of even the lower-income groups

<sup>10</sup> Another important objective, which is predominantly a matter for fiscal policy, is to minimize extreme inequalities in income and wealth.

and especially for better mobilizing such savings and directing them into more essential forms of investment. Finally, where real income per capita is rising, the associated increment of resources could be more fully mobilized for development.<sup>11</sup>

The problem of increasing and mobilizing real resources and of channeling them into expenditures serving the needs of balanced development—as well as the implementation of other measures designed to promote development—are primarily a responsibility of the government through its tax, expenditure, debt and other financial and economic policies. The formulation of the over-all development program itself is also primarily a government responsibility. The major objective and responsibility of the central bank should be to strive to achieve and maintain reasonable internal financial stability through control of the availability and cost of money. To the extent that the central bank is able, with the cooperation of the government, to achieve this objective, it will not only prevent the inequities and misuse of resources associated with inflation (or deflation), but also provide a necessary, though not sufficient, condition for increased saving, for attracting foreign investment and for promoting more balanced economic growth. As we shall see, the central bank can also contribute in other ways, within the framework of a policy aimed at stability, to encourage development. The maintenance of internal financial stability, it need hardly be added, would also help to foster, though not necessarily to assure, the maintenance of external payments stability as well.<sup>12</sup> External payments stability would in turn tend to facilitate the process of economic development.

The view has often been expressed in underdeveloped countries, though less frequently today and with usually a greater degree of sophistication, that the easiest and quickest way to accelerate development, given the difficulties of raising adequate resources through taxation, voluntary saving and foreign

<sup>11</sup> There are of course other potential sources of additional real resources for development, including utilization of underemployed or unemployed resources, mobilization of private hoards of gold and foreign exchange, larger foreign aid or investment, and improvements in the terms of trade. None of these can be relied upon, however, to any great extent.

<sup>12</sup> By external payments stability we refer to a situation where the average payments and receipts of a country on current and ordinary long-term capital account are in reasonable balance over the course of the cycle without resort to import quotas, exchange restrictions on current account or excessive tariffs.

capital, is by inducing forced saving through an inflationary expansion of central bank credit. The dangers of this argument have already been amply demonstrated by the experiences of many countries. Inflation invariably tends to promote the wrong kinds of investment by diverting resources into socially unproductive activities promising high speculative profits (e.g., inventories, real estate, foreign exchange), catering to luxury consumption or otherwise not contributing to balanced development. It upsets the balance of payments and leads to pressures on reserves. It discourages foreign investment. If carried far enough, it reduces the will to save. By shifting real income from the poor to the rich, it places a heavy burden on those least able to bear it and may weaken the social and political fabric. Beyond a certain point, moreover, inflation fails to elicit even the desired forced saving and tends to become cumulative. Under specified conditions, to be sure, plausible cases could be made out for a "certain" amount of inflationary financing of development—if it could properly be controlled—but such cases are relatively few. To conclude, therefore, a major objective of policy must be to attempt to see to it that development takes place within a framework of reasonable financial stability, i.e., that aggregate spending is kept within the limits of available real resources at current prices.

Obviously, the central bank alone cannot assure such stability. At best its role can be only a contributory one, however strategic that role might be. The financial policies of the government must carry a large part of the load. There must in any case be the closest possible coordination between the policies of the central bank and the government if there is to be hope of a job well done. For example, an irresponsible fiscal policy could easily upset the efforts of the central bank to maintain internal and external stability, just as an ill-advised monetary policy could counteract the effects of a prudent fiscal policy. Besides, trade, payments and exchange policies must be closely integrated with both, especially in the face of large and persisting imbalances in international payments.

While the achievement and maintenance of monetary stability is the dominant contribution that the central bank can make to balanced economic development in underdeveloped countries, it can also promote this objective in other ways.

Within the framework of a policy aimed at stability, it can seek to influence the flow of bank credit, and indeed of savings, in directions more in keeping with development ends. Thus, through selective credit controls applied to the banking system, through help in establishing and supporting special credit institutions and through influence over the lending policies of such institutions and of other institutional investors, it can help to some degree to rechannel real resources in desired directions, both between the public and the private sector, on the one hand, and within the private sector itself, on the other. The central bank can also play a useful role in increasing and mobilizing savings by helping to develop a market in government securities, by helping to establish special savings institutions, by encouraging a spread of banking facilities and of the banking habit, by promoting the liquidity and solvency of the banking system and by other related measures.<sup>13</sup>

In its attempt to maintain monetary stability, the central bank must constantly strive, despite the limitations to which it is subject, to adjust the aggregate money supply to the demands of the public for money balances at constant prices. These demands grow as the economy grows, thereby making possible a certain, though in most cases limited, rate of growth in the money supply without inflationary consequences. If the money supply is allowed to grow at a rate in excess of the public's demand for money at constant prices, there will be an upward pressure on prices; if it grows at a slower rate, there will be deflationary pressures and some retardation of production. In its attempt to keep the money supply growing at the "right" rate, however, the authorities will have to take account of undesirable developments that might occur in the balance of payments. If the pursuit of this goal involves large and persisting drains on exchange reserves, the authorities might have to slow up the rate of credit expansion; if it involves a large and persisting payments surplus, they might perhaps want to increase it.

Although the growth of real income is the major factor determining the public's demand for money, the rate of expansion in the money supply consistent with internal financial stability will not, of course, be exactly equal to the rate of growth of

<sup>13</sup> On all this, see below, pp. 261-269.



income. For one thing, the shrinkage of the non-monetary sector as the economy grows will in itself involve an increasing demand for money at constant prices. Moreover, the demand for money is likely to be stimulated by such factors as the growing differentiation of production, the spread of banking habits and the relative expansion of purely financial transactions. All these factors, which make for a decline in the income-velocity of money over time, would enable an expansion in the money supply at a rate somewhat greater than that of real income without inflationary consequences. On the other hand, when the public has little confidence that monetary stability can be maintained, there will be a move to economize on money holdings and the income-velocity of money will rise.

In its attempt to keep the money supply adjusted to the needs of the economy at constant prices, the central bank faces the special problem, noted in an earlier section, arising from wide externally induced swings in exchange reserves and in the money supply that occur from time to time in many underdeveloped countries.<sup>14</sup> These swings tend to disrupt the efforts of the central bank to maintain internal stability and militate against the steady course of economic development programs. Large externally induced surpluses in the balance of payments usually provide the economy with a greater amount of money than needed and tend to generate undesirable inflationary pressures. Conversely, large externally-induced deficits may involve undesirable deflationary pressures and a dangerous rate of drain on exchange reserves which would threaten to impair the country's ability to finance the imports of equipment and raw materials necessary for the continued implementation of the country's development program.

As noted earlier, there is little that the central bank can do by measures of credit policy to offset the primary expansions and contractions in the money supply resulting from such externally generated swings. To be sure, open-market sales or purchases of securities by the central bank to or from the *non-bank* public could, if substantial enough, help to offset these primary changes (and also the associated effect on commercial

<sup>14</sup> In the longer run, with the development and diversification of the economy, the absolute and relative importance of such swings is likely to be reduced and their internal effects to be more easily offset or absorbed.



bank reserves), but the securities market is invariably too narrow to enable such offsetting to be carried very far. In general, the central bank's main responsibility at such times should be to try to prevent the secondary changes in the money supply that would tend to occur. To the extent that an underdeveloped country *is* able to control the magnitude of externally induced swings in the balance of payments and their primary impact on the money supply and money incomes, the problem is predominantly one, not for credit policy, but for fiscal, payments and trade or exchange policy.

Before turning to some of the measures that might be taken, the question might be raised as to whether or not attempts at insulating the domestic economy from externally generated disturbances are invariably desirable. This would depend upon such considerations as the magnitude and probable duration of the disturbances, their probable internal effects in the absence of insulation measures, the size of the country's existing exchange reserves and the causes of the disturbances.<sup>15</sup> In view of these and other factors, which will vary from case to case, it is exceedingly difficult to lay down general rules.

As one general rule, however, it may be stated that where export booms are believed to be temporary, the authorities should attempt to minimize their inflationary impact on the economy, and the distortions which such impact would tend to create, and thereby to conserve as large a part as possible of the accruing foreign exchange receipts, which would otherwise tend to be partly drained away through enlarged imports, often of a relatively unessential character. When exports fall off and the balance of payments becomes adverse because of slackening world demand, the authorities should similarly try to maintain the level of internal incomes and to use the previously accumulated reserves to finance those deficits and to maintain the level of essential imports. On the other hand, when the externally induced shifts in the balance of payments are believed to reflect more permanent or structural forces,

<sup>15</sup> To the extent, for example, that a rise in export proceeds reflects a favorable movement in export prices, the authorities might want to permit some rise in domestic prices and money incomes as a means of enabling the higher real income associated with the improvement in the terms of trade to be distributed more widely throughout the economy instead of being concentrated in the export sector.

it might be desirable to allow them to exert their impact on internal prices, incomes and expenditures. Alternatively, the exchange rate might have to be adjusted, or the country's investment program reoriented, in the light of the altered international economic position—both of which would likewise have internal repercussions. Admittedly, however, it is not always easy for the authorities to determine whether the change in exports is likely to be temporary or not. It goes without saying, moreover, that, regardless of official attempts at insulation, some degree of inflation and deflation is inevitable in export economies in the face of major export booms and recessions emanating from abroad. National measures alone are insufficient.

It is not within the scope of this paper to discuss the various measures of fiscal, payments and trade, or exchange policy that might be taken by underdeveloped countries to minimize the domestic impact of externally generated fluctuations, or the relative effectiveness and desirability of each of these measures. A bare enumeration of some of these measures, which may be designed to act either on the money supply and money incomes or on the balance of payments itself, must suffice.

Suppose that there is a large increase in a country's exports, resulting from an increase in world demand and prices, the effects of which the authorities wish to counteract. Some part of the resulting increase in incomes and expenditures, and the foreign exchange counterpart, will automatically accrue to the government through taxes. The government must attempt to restrain its own expenditures and to sterilize the increased tax receipts in the Treasury's balance at the central bank, use them to repay debt to the central bank or use them to finance expenditures that were previously being financed by central bank credit. If the increased tax revenues were used to enlarge expenditures—as there would be a strong pressure to do at such times—their anti-inflationary effect would be dissipated. By imposing or raising export taxes, such as was done by Ceylon, India, Pakistan and a number of Latin American countries during the Korean boom, the government could absorb a still larger part of the increase in money and incomes; or taxes in general could be raised. Exporters might be forced to invest part of their increased incomes in special government securities,

as was done in Colombia and Brazil during World War II. Revisions in multiple exchange rate structures where they exist, i.e., widening the gap between export and import rates, would be another method of siphoning off to the government a further part of the increased money supply and incomes generated through the balance of payments. In countries where some exports are channeled through government marketing boards (e.g., Burma, Indonesia, Thailand and British African territories), such boards could absorb and sterilize all or part of the increase in export incomes without passing it on to those who produce for export. The government might act also directly on the export surplus itself by liberalizing its import and payments restrictions, where such exist, or by appreciating its exchange rate. In these and in other ways—not all of which are to be recommended—the authorities could reduce the internal impact of the export boom and, in most of these cases, also enable a larger part of the accruing foreign exchange to be added to official reserves for future needs.

One of the problems to which the government and the central bank must constantly be alert is the need for instituting appropriate corrective measures in the face of large and persisting drains on exchange reserves, however generated. At just what point such measures should be instituted, however, and just what measures should be taken (e.g., credit restriction, fiscal retrenchment, exchange depreciation, or imposition or tightening of trade and payments controls) are obviously highly difficult questions to answer in any given case. In an effort to provide a criterion or warning signal for policy in this respect, a number of the newer central bank statutes in underdeveloped countries impose central bank reserve requirements of a novel type;<sup>16</sup> and, when the ratios in question fall to a certain "critical" level, specific actions must be taken. In other cases, where no such requirements, novel or otherwise, are imposed, "guiding principles" are inserted in the statutes to assist the authorities in the timing and choice of corrective measures to meet reserve drains. Analogously, some of the statutes also

<sup>16</sup> E.g., central bank reserves are related to average sales of foreign exchange in a preceding period or to the volume of money held by the public. Such devices are confined entirely to certain Latin American central banks, such as those of Guatemala, the Dominican Republic and Ecuador. Experience with them, however, has not in general been satisfactory.

contain "guiding principles" or criteria for credit policy in the face of inflationary or deflationary movements at home.

While "criteria," "guiding principles" and "rules" are unquestionably of value in assisting the monetary authorities in the formulation and implementation of appropriate policies, especially in those underdeveloped countries where central banks were only recently established and where the requisite administrative skills and experience may be lacking, they cannot be expected to provide hard and fast rules to guide the authorities correctly under all possible circumstances. No formulas have as yet been discovered to assure appropriate monetary policy in all cases. There is no substitute in any given situation for sound and informed judgment, reached on the basis of a detailed examination and understanding of all available facts and criteria of relevance, and growing out of the lessons of experience.

#### INSTRUMENTS OF CREDIT CONTROL IN UNDERDEVELOPED COUNTRIES

We turn now to a discussion of the various instruments of general and selective credit control that have been employed by central banks in underdeveloped countries in recent years.

The scope for open-market operations in most underdeveloped countries, especially as an instrument of credit restraint, is narrowly limited for reasons mentioned earlier. Although the majority of central banks in underdeveloped countries are formally equipped with the power to engage in such operations, in most cases this power has been relatively inoperative.

Where open-market operations have been undertaken, they have usually been on the buying side. In some cases (e.g., Mexico and the Philippines), purchases appear to have been dictated mainly by a desire to support securities prices and thereby to encourage the growth of a market, rather than by a desire to influence the availability and cost of credit as such. In some cases, they have been undertaken as a means of providing reserves to *specific* banks or government lending agencies (the latter are often permitted to issue their own securities under government guarantee). In further instances, they have been made in keeping with the objectives of a deliberate cheap money policy (e.g., India up to the end of 1951) or to prepare

the market for government flotations. Open-market sales, where such have been effected (e.g., Ceylon and, since 1951, India), have usually been relatively small and infrequent. For, even when measures of credit restraint are called for, there has been an understandable reluctance on the part of the central bank to sell in a narrow market and to depress securities prices unduly. It is widely recognized that a market must first be developed before open-market operations can become an effective means of implementing monetary policy.

This has been formally recognized by the inclusion of special provisions in the statutes of some of the newer central banks in underdeveloped countries. For example, the central bank statutes of the Dominican Republic, Guatemala, the Philippines, Ecuador and Honduras, among others, provide for the establishment of special "securities stabilization funds" to be administered by the central bank and to be used for open-market operations designed to increase the liquidity of government securities by preventing or moderating sharp price fluctuations. The injunction is usually laid down, however, that these funds should not be used to resist basic market trends. In actual practice, however, these funds have rarely been used. In at least two cases, their basic purpose has been perverted by the purchase of securities directly from the government.

Some of the newer central bank statutes also empower the central bank to issue its own securities for purposes of open-market operations in order to meet situations where its holdings of government securities are insufficient or where such securities do not carry maturities or other terms attractive to the market. The Central Bank of Ceylon has recently issued its own securities under such a provision.<sup>17</sup>

Discount operations have likewise not been of much significance in the majority of underdeveloped countries as an instrument through which the central bank has been able to influence the availability and cost of credit. In many of these countries, especially in Asia and the Middle East, the reserves of the commercial banks are usually so ample as to preclude the need for any regular recourse to central bank credit via

<sup>17</sup> During the late thirties, the Central Bank of Argentina had also issued its own securities.

rediscounts and borrowings.<sup>18</sup> In periods of inflationary pressure when measures of credit restraint are called for, moreover, the banks are often being fed liberally with additional reserves through the balance of payments or government borrowings at the central bank. Foreign-owned commercial banks usually prefer to replenish their reserves when necessary by borrowing from their head offices abroad or by rediscounting their holdings of trade bills in foreign money markets where this is possible. In some cases where banks would like short-term accommodation from the central bank, they might be hampered by insufficient holdings of paper eligible for rediscounting or borrowing, despite the relatively generous provisions governing such accommodation in many of the central bank statutes. Finally, the underdeveloped state of the money and capital markets, and the absence in most cases of any long-standing tradition of central bank leadership or of conventional arrangements, tend to make rates of interest in the organized sector of the market relatively insensitive in most cases to changes in central bank discount rates. With the growth of the economy, however, the force of these various obstacles should progressively abate.

Changes in central bank discount rates in most underdeveloped countries have in actual practice been relatively infrequent. Although it is extremely difficult to generalize about the effects of such changes, the evidence at hand does not suggest that they had any pronounced effects in the majority of cases upon the volume of commercial bank rediscounts and borrowings at the central bank, upon commercial bank loan rates or other market rates or upon the volume of commercial bank loans to their own customers. Even less does the unorganized sector of the money market appear to have been influenced by changes in central bank discount rates.

In this connection it is worth noting that many of the central banks, especially in Latin America, do not have a "single" discount rate, but, in an effort to exert a measure of selective credit control, have a number of rates according to different kinds of paper eligible for rediscount or as collateral against

<sup>18</sup> As noted earlier, this degree of liquidity is often a reflection in part of the absence of a tradition of borrowing at the central bank. It might also be noted that specialized government financing institutions in some cases rely on central bank credit to a greater extent than do the commercial banks.



borrowings. In such cases, there is usually a "general" or "basic" rate, which may often remain fixed while changes are made in various of the individual rates. Rarely are all rates changed at the same time in the same direction or to the same degree. Some measure of selectivity is also sought in many cases by different eligibility requirements for different types of paper.

In those underdeveloped countries where the banks *do* rely to a significant degree upon central bank credit,<sup>19</sup> the effectiveness of discount operations as an instrument of credit control is likely to lie, not so much in changes in discount rates, as in changes in the availability of credit. For the central bank, by rationing its credit (e.g., by rediscount quotas or ceilings), is able to exert a direct quantitative influence on the loan potential of banking institutions. By rationing credit selectively according to various types of paper, moreover, the central bank may be able to some degree to influence the character of the loans of such institutions.

An interesting and unusual example of the use of the discount mechanism as an instrument of credit control in underdeveloped countries is provided by recent Japanese experience. Under a complicated so-called "higher interest rates application system," the Bank of Japan fixes lines of credit for the different banks depending upon the amount of their own resources, their borrowings from the Bank and other factors. A series of differential "basic" rates, related to various types of eligible paper, are applied to an initial portion of the credit line in each case. Borrowings above that portion, but within the credit line, are subject to differential rates in excess of these "basic" rates; and borrowings above the credit line are subject to still higher rates. From time to time, the Bank of Japan in recent years has not only altered these various rates but also changed the portions of the credit line to which they apply. In this way it has been able to exert a considerable influence on bank lending policies, given the heavy dependence of the banks on central bank credit and the fact that the interest rates charged by the banks to their customers are fixed under law.

A large number of central banks in underdeveloped countries

<sup>19</sup> See footnote 8 above, p. 241.



have the power to vary the legal reserve requirements of banking institutions within a substantial range. In those developed countries where such power exists, changes in reserve requirements are usually regarded as a somewhat blunt instrument of general credit control, to be used relatively infrequently when needed to wipe out or to release at a stroke a large block of excess reserves and, incidentally, to reduce or increase the deposit-creating capacity of the commercial banks on the basis of any given amount of reserves. In underdeveloped countries, on the other hand, given the relative ineffectiveness of open-market and discount operations and the wide swings in bank reserves, resort to this device may have to be had more frequently, notably on occasions when reserves are rising unduly because of inflows of foreign exchange or central bank-financed budget deficits. In many cases, however, the increases in reserve requirements may have to be very substantial if they are to impinge significantly upon the liquidity positions of the banks.

Changes in reserve requirements may often involve serious inequities, since they strike alike at banks with large and with small excess reserves and at banks which are expanding credit rapidly and at those which are not. An alternative method, which many of the newer central banks are also empowered to undertake, would be the imposition in periods of rapidly rising bank reserves of very high supplementary reserve requirements against *increases* in deposits, while leaving the regular requirements unchanged. This would avoid the above-mentioned inequities and also strike more directly at the root of the problem. If, in the extreme case, the supplementary ratio were fixed at 100 per cent, the commercial banks could theoretically expand their loans and investments only to the extent that they already had excess reserves, which they were willing to use, or could get reserves by borrowing at, or selling holdings of securities to, the central bank or by repatriating their pre-existing foreign exchange assets. Even in these cases there could be only a one-to-one expansion in bank loans and investments relative to reserves.

A number of central banks, including, among others, Mexico, Colombia, Ecuador, Ceylon, Bolivia, South Korea and Peru, have from time to time varied their ordinary reserve require-

ments upwards and/or downwards as a means of inducing general credit restraint or ease. In addition, Mexico, Colombia, Brazil, Israel and Peru have imposed high supplementary requirements against deposit increases. Experience with these devices, especially in Mexico and Colombia which have made most use of them, has indicated their considerable potentialities as control instruments, although in some cases their effectiveness has been hampered by the tendency of the banks to hold large excess reserves.

Some central banks, such as those of Chile, Israel, Mexico, Uruguay and the Philippines, have also used reserve requirements for selective credit control purposes. In these countries, banking institutions have been permitted to count certain earning assets, usually government securities and certain categories of "productive" loans, as part of their legal reserves in an effort to encourage them to extend credit in directions favored by the authorities and to promote the development of a government securities market.

Among other instruments of credit control at the disposal of various central banks in underdeveloped countries is the power to impose ceilings on the loans and investments of the commercial banks or on the rate of increase of such assets within specified periods of time. This instrument can also be used as a selective credit control device to check the growth of specific categories of loans and investments as compared with others. As a weapon of quantitative control, the portfolio ceiling device would seem to be recommended mainly for situations of extreme emergency when all other, less direct, methods of stopping or slowing up a dangerous expansion have failed or are likely to fail. For it involves an objectionable degree of direct interference in bank loan and investment policies and may also involve serious inequities as among individual banks. A number of countries, notably South Korea, Mexico, Colombia, Bolivia, Chile, and Costa Rica, have resorted to this device for limited or more extended periods of time. In at least two of these cases, however, it has proved to be of little avail in stopping or even slowing up an inflationary expansion of bank credit, since the ceilings have been fixed at levels allowing too much room for expansion or have been raised too frequently.

Other methods have been used in an attempt to exert a measure of general or selective credit control. Moral suasion, in the form of formal or informal requests to banking institutions, has undoubtedly been widely resorted to, although the results are obviously difficult to assess in general terms. A large number of countries, including among others the Philippines, Pakistan, Colombia, Nicaragua, Indonesia, Ecuador and Uruguay, have relied at times of inflationary pressures upon the device of fixing prior deposit requirements for imports<sup>20</sup> or minimum cash margins for the opening of import letters of credit in an effort to restrain the demand for imports or specified types of imports and also to exert some anti-inflationary effect. In those countries where the central bank engages in a commercial banking business, which is substantial in relation to total bank loans to the private sector (e.g., Bolivia, Chile, Colombia, Ecuador, Nicaragua, Uruguay, Egypt, Iran and Ethiopia), variations in the central bank's loans to the public have sometimes been used with effectiveness to exert a desired degree of influence on the total credit volume. Frequently, however, the bank's lending to the public has contributed to, rather than alleviated, an undesirable over-all expansion of credit. In some countries (e.g., Chile, Bolivia and Paraguay), the central bank has tried to restrain credit by requiring all commercial bank loans to individual customers above a certain amount to be first submitted to it for prior approval. The shifting of Treasury deposits between the central bank and the commercial banks may in some cases have been deliberately undertaken to induce a desired measure of credit ease or restraint, although such shifts appear to have often been motivated solely for political reasons. To stimulate lending institutions to make certain types of socially desirable loans to the private sector, at least one central bank (namely, in the Philippines) has introduced a scheme whereby it agrees to guarantee the repayment of such loans up to a specified percentage.<sup>21</sup>

<sup>20</sup> I.e., importers are obliged, at the time of applying for an import license, to deposit with the central bank a specified part of the local-currency cost of the imports.

<sup>21</sup> Two underdeveloped countries, namely, Indonesia (1950) and South Korea (1953), have in recent years resorted to the extraordinary measure of a monetary "purge" in order to wipe out excessive liquidity in the hands of the public. In

It will be observed that many of the credit control measures discussed in the foregoing paragraphs are of a selective character designed to encourage or discourage specific types of bank loans and investments and thus to influence the allocation of bank credit and of real resources in desired directions. Many underdeveloped countries, in fact, have been much more concerned with such measures than they have been with general credit controls. The specific objectives sought by the use of selective credit controls have been many: to discourage credit for speculative or relatively unessential purposes and to encourage it for more socially productive ones; to meet more adequately the credit needs of specific sectors of the economy which cannot obtain sufficient bank credit at reasonable cost; to meet more adequately the needs for specific types of credit (e.g., medium- and long-term credit), even in relatively well-organized sectors of the economy; to assist in discouraging excessive or unessential imports; to counteract, without the need for stronger general credit measures, an inflationary movement which is being significantly promoted by excessive credit to one or a few specialized sectors of the economy (or to shelter certain sectors from the effects of restrictive general credit policies); to assist in developing a government securities market; or to promote economic diversification as such. Nearly all of these objectives, it might be noted, are directly or indirectly related to the broader objective of promoting balanced economic growth.

With such a variety of objectives, and with such a diversity of measures used, it is exceedingly difficult to draw any general conclusions as to the degree of effectiveness that selective credit controls may have had in underdeveloped countries in achieving the objectives sought. These controls have probably been more effective in influencing the distribution of bank credit between the private and public sectors than they have been in influencing the distribution of credit within the private sector itself. In the latter case, the effectiveness of these controls has tended to be limited by a number of well-known factors that require no detailed elaboration.

For one thing, even if selective credit controls were effective

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both cases, however, given the continuance of underlying inflationary forces, the effects were only temporary.

in discouraging undesirable types of commercial bank credit, there is no necessary assurance that the banks would want to use the resources so freed to expand credit in the desired directions or indeed that borrowers would want to expand their borrowings in these directions. Even if these controls, moreover, *were* formally effective in influencing the allocation of bank credit in keeping with the wishes of the authorities, there is no necessary assurance that the redistribution of bank credit would involve a corresponding redistribution of expenditures with the borrowed funds. For example, it would in most cases be relatively easy for a borrower, especially if he engages in a number of activities simultaneously, formally to borrow for the "permitted" purposes but to use the funds in actual practice for "non-permitted" ones.<sup>22</sup> Or, by borrowing more heavily for the "permitted" purposes, he would thereby be enabled to free his own resources for "non-permitted" expenditures. "Leakages" may also occur because of the administrative difficulty in most cases of defining different types of bank loans and investments in precise operational terms and of determining whether any given type of loan is involved in any given case. When selective credit controls are undertaken in periods of inflationary pressure, their effectiveness is sometimes weakened by the absence or inadequacy of supporting measures of general credit restraint. Finally, it should be recalled that bank credit is not the only source of borrowings for private investment or other expenditures (although in underdeveloped countries it is usually the most important one). Borrowers to some degree may tap the capital market (however limited it might be) or resort to moneylenders.

Although the experience of underdeveloped countries, as discussed above, provides many illustrations of resort to various measures of general and selective credit control, it must be emphasized that the central banks in most of these countries, especially in the Middle East and in Asia and the Far East, have made in general relatively limited use of the various instruments of control at their disposal. This should not necessarily be regarded as to the discredit of the central banks con-

<sup>22</sup> Analogously, where the selective credit controls take the form of a selective rediscount policy by the central bank, a bank may borrow against one kind of paper but lend the proceeds to its customers against another.

cerned. The over-all potentialities of many of these instruments are narrowly limited, as we have seen, by institutional factors, and it is not self-evident that more vigorous measures of credit restraint would in most cases have significantly altered the course of events. Some of these instruments, despite the intentions of the drafters of the statutes, are not too well adapted to the financial structures and administrative capacities of the countries concerned and are in fact of so complex and novel a character as to justify scepticism regarding their use. Some, moreover, were designed to meet special or emergency situations of a sort that have not as yet emerged in many of these countries.

Despite all this, there is reason to believe that on certain occasions, notably during the Korean boom of 1950-51, there was in at least some cases scope for more aggressive measures of credit restraint than were actually undertaken. There were a number of reasons for this hesitancy. Measures of credit restraint are never popular and most central banks were under strong pressures from the business community and often from the government itself to avoid restrictive measures. Since many of these banks are relatively new and have yet to establish the degree of standing and prestige necessary to make their views and their leadership in monetary matters appropriately felt in the community—or in fact to make their legal position secure—it was often understandably difficult to resist such pressures. In some cases, as intimated above, there was undoubtedly uncertainty as to what instruments to use, how to use them or how effective they might be. But perhaps of greatest importance was the fear by many central bank officials that restrictive monetary measures might hamper the progress of economic development itself. In countries where growth is the primary objective of national economic policy, such a fear tends to be all too deeply rooted. In some countries, moreover, the "old-fashioned" notion still prevails that so long as bank loans are made for "productive" purposes and to meet the "needs of trade" there cannot even be a danger of inflation.

It is impossible here to attempt any over-all evaluation of the effectiveness of such credit-control measures as have actually been undertaken in underdeveloped countries in recent years. Experience has naturally varied widely from country to



country according to the particular circumstances. Most of the central banks concerned seem in the main to have been groping their way and cautiously experimenting with various credit-control techniques in an effort to determine their relative effectiveness and suitability under differing conditions and to test their adaptability to the local environment. In these respects they have received and can expect to receive only relatively little guidance from the lessons, experiences and philosophy of central banking in the more developed countries.

#### MONETARY POLICY AND ECONOMIC DEVELOPMENT

In earlier sections there was a discussion of various ways in which monetary policy could contribute to balanced and orderly economic growth in underdeveloped countries, especially by helping to maintain internal and external stability and by measures of selective credit control designed to channel bank credit in desired directions. This section will deal with other measures of central bank action, for the most part of a "non-traditional" sort, that might help to promote the over-all development of the economy and a greater effectiveness of monetary policy itself. Such measures would be justified, however, only to the extent that they do not conflict with the requirements of financial stability and do not enmesh the central bank in details of a sort that might distract its attention and energies from the effective implementation of a policy aimed at stability.

Selective credit controls, as already noted, face a number of limitations as an instrument for redistributing bank credit and real resources, especially from the viewpoint of their ability to *encourage* a flow of bank credit of desired types or in desired directions. It is evident that if credit is to be redirected in a way more in keeping with the requirements of balanced development, other measures are also needed.

It is sometimes argued that the central bank should itself engage in a banking business with the public so as to meet those essential credit needs which are inadequately provided for under existing institutional arrangements.<sup>23</sup> Although this argument may have some force under certain conditions, there

<sup>23</sup> In some cases, moreover, as noted earlier, central bank dealings with the public could provide a useful instrument of general credit control.



are good reasons why central banks should not, in general, deal with the public, and why the great majority of them do not. Experience has demonstrated that such activity, if carried out on a substantial scale, has frequently tended to divert the central bank's energies from its primary over-all regulatory responsibility, to subject it to added pressures to extend credit too liberally and to contribute to inflationary developments. To the extent, moreover, that dealings with the public have brought the central bank into direct competition with the commercial banks, such competition has tended to arouse suspicion and animosity in the banking community and to impair the central bank's prestige and its ability to make its monetary policy felt.

A more attractive alternative would be to establish special institutions for the specific purpose of providing some of the needed credit facilities. For example, in a number of underdeveloped countries (e.g., Pakistan and Burma), the central bank has cooperated with the government in helping to set up and to provide a measure of support to state-owned commercial banks designed to provide short-term credit to sectors of the economy not adequately serviced by private commercial banks. Of more importance in underdeveloped countries, however, is the shortage of medium- and long-term credit, and of long-term finance generally, for industry and agriculture. In an attempt to repair this deficiency, the majority of underdeveloped countries, often with central bank help, have established official or semi-official industrial and agricultural development banks, development corporations or other long-term financing institutions.

It is difficult to generalize about the nature of such institutions in view of the wide diversities characterizing them. In general, their activities mainly comprise: extending medium- and long-term credits (and sometimes short-term credits) to industry and agriculture; participating in the capital and management of existing or newly-formed enterprises; directly undertaking development activities themselves in various fields; or any combination of these. The sources of their funds, which likewise vary from case to case, include: initial capital subscriptions and/or annual appropriations from the government; proceeds from sales of shares or debentures to the public,

including commercial banks and institutional investors; foreign capital (public and private); retained profits from operations; receipt of long-term deposits, allotments from counterpart funds; borrowings and discounts from, or sale of shares and debentures to, the central bank; or any combination of these.

It is similarly difficult to generalize about the experiences of these institutions. Too often, perhaps, especially in the case of certain Latin American countries, the operations of these institutions have had the effect of causing or aggravating inflationary pressures by involving excessive reliance upon direct central bank credit or upon government funds themselves obtained from the central bank. On the other hand, in countries where financial affairs in general are conservatively managed, these institutions have frequently suffered from an inadequacy of funds to carry out their objectives because of an inability to mobilize a significant amount of private savings or to obtain sufficient funds from the government or the central bank. Between these two extremes, there are many countries in which these institutions have played a valuable role in channeling public and private savings into development projects, while avoiding undue reliance on central bank credit.

Within the limits on over-all credit expansion imposed by a policy aiming at reasonable monetary stability, the central bank can play an important role in the organization and successful operation of these institutions by contributing part of their initial capital and by supplementing their resources from time to time through loans and discounts and purchases of debentures. If such financial aid goes beyond these limits, however, it becomes merely another means of promoting inflation. The problem of how to keep central bank financing of official financing institutions within the appropriate limits merges into the larger problem of how to avoid excessive central bank credit to the government generally. If the government, in its zeal to accelerate economic development, insists, despite central bank remonstrance, upon pursuing irresponsible financial policies necessitating undue resort to the central bank by the government or by its instrumentalities, in the final analysis there is nothing that the central bank can do but to yield. The ultimate responsibility thus lies with the government in

such circumstances if the central bank is unable to maintain monetary stability.<sup>24</sup>

It is not enough in most cases for the central bank to try to influence the lending operations of official development institutions by control over its loans and discounts to, and its purchases of the securities of, such institutions. Even when central bank credit is not involved, variations in the rate and timing of these lending operations can have very important effects on the level of aggregate spending and economic activity. Such operations must thus be closely coordinated with the monetary policy of the central bank so that the two do not pull in opposite directions, as has happened in the past in many Latin American countries. In an attempt to achieve such coordination in a formal way, there has been an increasing tendency for officials of the central bank to be represented on the managing boards of such institutions, e.g., Cuba, Guatemala, Honduras and Ethiopia, or conversely, the Philippines. In some cases, moreover, the central bank has more direct powers over their lending operations, analogous to some of those which it exercises over the commercial banks.

A related problem is that of exerting some measure of control over the investment policies of insurance companies, savings banks, mortgage companies, pension funds and other, usually privately-managed, collective savings institutions—at least in those underdeveloped countries, notably certain Latin American countries, where the savings at the disposal of these institutions are quantitatively significant. For such savings often tend to be invested unduly in fields not contributing to balanced economic development. In an attempt to redirect these savings, some countries have compelled insurance companies or others of these institutions to invest a certain percentage of their resources in government securities. In some cases, moreover, these institutions, especially savings banks, are subject to the broad supervision of the managing board of the central bank. Such measures might perhaps be extended to a larger number of countries; and in some cases a greater degree of supervision and control, of a sort that might properly

<sup>24</sup> This is certainly not to imply, of course, that the central bank is always unsuccessful in its efforts to persuade the government as to the appropriate financial policies to be pursued.

be undertaken by the central bank, might be desirable. Thus, for example, the central bank might be given the power to fix maximum limits upon the amount of the annual increase in the resources of collective savings institutions that might be invested in various ways, e.g., real estate.

Mention has already been made of the fact that commercial banks in underdeveloped countries, because of their traditional concern for a very high degree of liquidity, concentrate predominantly on short-term loans to finance commercial transactions and engage to only a very limited extent in longer-term loans to finance industrial and agricultural expansion. There can be no doubt that this degree of concentration has been overdone in many cases. The over-all liquidity of commercial banks is usually so ample that at least some degree of redirection of credit towards longer-term loans—without involving a reduction in legitimate demands for short-term credit—should not endanger bank positions.<sup>25</sup> Provided that the *over-all* volume of commercial bank credit were kept within the appropriate limits by central bank action, some such degree of redirection would seem justified in the interests of economic development.

It is not likely, however, that the central bank can do much, given traditional banking habits, to stimulate a larger volume of longer-term commercial bank loans in the near future. Selective credit controls, as indicated, are not likely in general to be very effective, but some stimulus might be given by central bank guarantees of such loans, use of differential reserve requirements, lengthening the maturities of paper eligible for central bank rediscounting or assurances that the central bank would stand ready to help the banks in the event of large and sudden deposit withdrawals. Liberalization of restrictions imposed by some general banking laws upon the maximum maturities of commercial bank loans might also be helpful in such cases. In general, however, private longer-term credit needs will have to be satisfied predominantly through the establishment of official credit institutions, such as discussed above.

A special financing problem in underdeveloped countries is invariably posed by agriculture. Here the risks and costs of

<sup>25</sup> It would be almost superfluous to point out that confining loans to short-term, "self-liquidating" transactions, as such, is in any case no assurance against illiquidity.

granting loans, whether short-, medium- or long-term, are especially great, not only because of the large number of small individual debt-ridden farmers, whose standard of living is very low and whose level of education and technical knowledge is very limited, but also because of the natural hazards of farming, the frequent absence of clear titles to land or other acceptable loan collateral, and poor systems of farm tenancy. Except perhaps for loans to large plantation owners, commercial banks have generally avoided the financing of agricultural production. The specialized official agricultural banks which have been set up have generally been able to satisfy only a small part of the credit needs of small farmers. Cooperative credit societies and rural credit associations, while common in underdeveloped countries, as yet play only an exceedingly modest role. The moneylender, as a result, continues to be the main source of agricultural finance.

This is another area where, in the interests of the over-all development of the economy, the central bank can play a potentially useful though essentially limited role. The Reserve Bank of India provides an interesting example of a central bank that has devoted special attention to this problem. It provides rediscount facilities on favorable terms to the central cooperative banks. It has subscribed to the guaranteed debentures of land mortgage banks. It has established a special department within the bank to make a continuous study of methods of improving rural credit facilities. It has encouraged and assisted the extension of cooperative facilities. By and large, however, this is a problem for the government, not only by channeling public savings into agricultural banks and by legislation designed to improve systems of land tenure, but also by broader measures to improve the economic lot of the small farmer and to raise his standards of literacy, health and productivity.

Another important field for central bank action in mobilizing and channeling savings would be to assist in developing a market in government securities. The central bank could play a useful role in this respect, not only by helping to maintain internal financial stability, but in other ways. It can advise the government on the appropriate timing of its issues and on the fixing of interest, maturity and other terms designed to appeal to the different classes of potential investors, and it can

assist in the underwriting of various issues. By judicious operations in the open market to prevent undue price fluctuations, although without attempting to resist basic market trends, it can help to reduce fears as to the liquidity of government securities. It might permit government securities to be counted as part of commercial bank legal reserves, thereby encouraging the banks to hold a larger amount of such securities. Finally, it can assist in a more aggressive educational and selling campaign to widen the market for securities. In certain underdeveloped countries, notably Mexico, Cuba, Ceylon, India and the Philippines, the central bank in some of these ways has already contributed substantially to the growth of a market. In general, however, relatively little if anything has been accomplished in this respect, and the process will inevitably be slow.

With regard to central bank open-market purchases designed to enhance the liquidity of government securities, such support operations, if too rigid, might of course at times run counter to the need for pursuing a policy of credit restraint. In such cases—if the central bank does not wish to discontinue these operations or to “back away”—the problem might conceivably be met by attempting to immobilize the added commercial bank reserves through the imposition of high supplementary reserve requirements or even by the imposition of loan ceilings. It might also be noted that support operations can sometimes degenerate into a vehicle for indirect financing of government deficits.

Mexico has probably carried support operations further than any other underdeveloped country as a means of encouraging the growth of a securities market. The Bank of Mexico has directly or indirectly supported at par or close to par the prices of the securities of the government, of some official credit institutions, and indeed of some private institutions. Some securities, moreover, notably those of the national development corporation—the *Nacional Financiera*—have in effect been redeemable on demand; and such redemptions have been made possible by credits from the Bank of Mexico. While such support and redemption policies have had the desired effect of making the securities very liquid and of encouraging investment in them, they have at times interfered with policies of



credit restraint,<sup>26</sup> and, of more importance, have in effect forced the Bank of Mexico to extend credit to finance capital flight whenever the local currency was under pressure. Recently, however, steps have been taken to permit a greater measure of flexibility in securities prices.<sup>27</sup>

Finally, the central bank can contribute in other less direct but nonetheless important ways to the over-all development of the economy. It can help to establish special savings institutions, especially in rural areas, for the purpose of mobilizing such small savings as are currently taking place and indeed of stimulating savings habits.<sup>28</sup> It can encourage and assist commercial banks to extend their branches into such areas so as to bring banking facilities to a larger part of the population. It can try to encourage a wider use of money in the non-monetary sector of the economy. It can help to improve the efficiency of the payments mechanism within the country. It can attempt to effect a better coordination between the organized and unorganized sectors of the money market so that its monetary policy can be diffused more speedily and effectively over the country as a whole. It can seek, through the powers of bank supervision and examination which are usually entrusted to it, to promote sounder banking practices in the interests of greater bank liquidity and solvency. As a center for research, it can help to improve the country's statistical services and to further public enlightenment on economic and financial matters. Last, but not least, in its role as fiscal adviser to the government, it can help to promote sound fiscal policies and practices. Indeed, such measures as these, undramatic though they appear,

<sup>26</sup> This problem has apparently arisen, not so much because of the difficulty of restraining commercial bank credit (since high reserve requirements are imposed), but because of the fact that the *non-bank* public is a substantial holder of government securities, especially those of the *Nacional Financiera*. When an attempt is made to restrain credit, the public can quickly turn such holdings into cash.

<sup>27</sup> Some central banks, notably India, have taken measures to develop a market in *commercial bills*. Under a scheme introduced in January 1952, the Reserve Bank of India encouraged the banks to arrange with their customers to convert part of their loans and overdrafts into 90-day bills or promissory notes by offering (1) to make advances to the banks on the security of such paper at  $\frac{1}{2}$  per cent below the bank rate and (2) to bear half of the cost of the stamp duty incurred in such conversions. (Some adjustments were made in this scheme early in 1956.) Similar measures to foster the use of commercial bills were taken by Pakistan and Burma.

<sup>28</sup> One must be on guard, however, against assuming that a mere multiplication of savings institutions will in itself solve the problem of inadequate savings.



might well be among the most important that the central bank can perform in the near future in many of the more underdeveloped countries.

#### CONCLUDING REMARKS

Despite the impressive array of instruments at its disposal, and the seemingly wide range of tasks that it might perform, monetary policy in the great majority of underdeveloped countries has been, and of necessity must be, relatively limited in role, scope, and effectiveness in view of the many institutional obstacles which it faces. Even in developed countries, monetary policy is subject to many limitations; in underdeveloped countries the limitations are multiplied many times over. Effective control by the central bank over the money supply tends to be impeded by wide externally generated swings in the balance of payments and, at times, by the difficulty of resisting excessively large demands for central bank credit by the government and its instrumentalities; some of the tools of monetary control, even over that (often relatively small) segment of the money supply most directly susceptible to central bank influence, are subject to technical limitations; the response to monetary-policy measures is often likely to be relatively slow and uncertain; and some parts of the economy are in fact virtually outside the reach of central bank action. Besides, fiscal policy, which needs to be so closely coordinated with monetary policy, is itself subject in most underdeveloped countries to severe limitations, which are likewise inherent in the economic backwardness of these countries.

On the other hand, there is a danger of underestimating the potentialities of monetary policy in underdeveloped countries. As this paper has tried to show, there is still a constructive role for monetary policy to perform in the majority of these countries in helping to maintain internal and external stability, to promote economic development, and to lay the basis for a more effective application of its tools in the future. Indeed, there is reason to believe that most of these countries have not as yet fully utilized the potentialities of monetary policy, however limited they might now be.

A key problem in the formulation and implementation of appropriate monetary policies lies in the nature of the relation-

ship between the central bank and the government. All too often in the past, such policies have been hampered or thwarted in underdeveloped countries by excessive political interference in the operations and policies of the central bank and by undue government recourse to central bank credit. These problems cannot be solved merely by legislation or by formal administrative arrangements. A heavy responsibility devolves upon the government. It goes without saying that the government must try to order its fiscal affairs so as to keep its resort to central bank credit within the appropriate limits. Although the government and the central bank must of necessity be in close and continuous consultation on a wide range of matters, effective monetary policy also requires that the central bank should exercise, and be encouraged by the government to exercise, a wide measure of freedom in policy-making, in operations, and in independently developing and expounding its own point of view on the basis of its objective appraisal of the situation at hand, freed from short-run political pressures which may often conflict with the long-run welfare of the economy. The central bank should also have the maximum degree of freedom to comment upon and to criticize the government's fiscal and over-all economic policies and objectives and to try to the best of its ability to convince the government of its views. Such freedom would also help to promote the bank's prestige in the community and its position of leadership in monetary matters, so necessary to make its policies effective.

The argument has been raised that the establishment of central banks in some of the more underdeveloped countries was premature and that it would have been better if the previously existing monetary arrangements, which permitted little or no scope for monetary policy, had been left unaltered. It is difficult to accept this view. Apart from the fact that political considerations invariably made the establishment of a central bank inevitable in such instances, all of the countries in question have reached a stage of economic development—including a degree of monetization of the economy and of growth of the domestically oriented sector—where there is at least some scope for constructive central bank action.

Perhaps a more valid criticism is that many of the central bank statutes in underdeveloped countries are unduly

complicated and contain too many "fancy gimmicks" of a sort not too well adapted, despite the intentions of the drafters of the statutes, to the financial structures and especially to the administrative capacities of the countries concerned. Admittedly, simpler statutes would in most cases have been preferable, and some of the more recent statutes are in fact of this kind. In any case, there is no necessary obligation imposed upon the central bank to use all of these more complicated provisions, some of which were actually designed for "emergency" or more distant situations.

Another criticism has centered on the danger of misuse of the powers inherent in the establishment of central banks in underdeveloped countries, especially that of government access to central bank credit. In some cases, admittedly, the central bank has served on balance as little more than an engine of inflation. But this risk is in general much more than outweighed by the stabilizing influence, developmental contribution and other benefits that such an institution, under wise management and with appropriate cooperation from the government, should be able to bring to the countries in question. Most of the newer central banks have in fact already demonstrated their ability and potentialities in this respect, despite the many limitations and obstacles which they, and indeed central banks in underdeveloped countries in general, face and will continue to face for some time to come.

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## CONTEMPORARY VIEWS OF THE DOLLAR PROBLEM

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IT is the purpose of this paper to analyze critically the contributions made to the discussion of the "dollar problem" by eleven economists in the last two years. We shall try to discover what contributions were made by these economists to four topics: 1. the definition of the dollar shortage; 2. an answer to the question whether there still exists a dollar problem today; 3. an interpretation of the causes of the long-run or "chronic" dollar problem; 4. and policy recommendations.

### DEFINITIONS OF THE DOLLAR PROBLEM

Everyone seems to agree that the dollar problem basically consists of the non-North American world spending more in North America than it earns and receives in loans and investments from that area. Some economists, by elaborating on the basic definition, immediately give a hint as to where they suspect the cause to lie, or they want to make sure that a real problem exists even if under a straightforward definition a balance seems established. Thus, for example, it might be claimed that to a surface balance there should be added the requirement of no discriminatory barriers to American goods, a high and free level of trade (i.e. with no abnormal restraints), relatively high employment, and "reasonable" terms of trade between America and the rest of the world. A dollar problem can therefore still exist when currencies are convertible, since convertibility can be maintained at the expense of heavy unemployment in the rest of the world (as was the case in the 1930's) and/or serious import restrictions against American goods.

There are some economists who object to a definition of the problem that includes more than just the straight market view, that is, one which is related to the achievement of certain objectives. By this is meant that the existing shortage could be eliminated by way of operation on internal incomes and prices

<sup>1</sup> This is an abridged version of a paper originally presented at the International Trade Seminar of Professors Haberler and Harris in 1955.



in order to dampen excess demand, by way of exchange rate manipulations or by import and exchange control. But this is not done in order to avoid social unrest. Thus, the dollar shortage is defined in the light of attaining a "political equilibrium." It is thought that equilibrium beyond the market would be too subjective and vague a definition.

#### DOES THE DOLLAR PROBLEM STILL EXIST?

The equilibrating tendencies since the middle of 1952 have led many to ask whether the dollar problem was not a thing of the past. Since the second half of 1952 the current account of the U. S. balance of payments has been practically in equilibrium; the imports and exports of goods and services of the U. S. have been almost exactly balanced and there has even been a small trickle of private capital exports from the U. S. and a substantial, though somewhat reduced, U. S. government aid. This seeming normalization of the balance of payments was due mainly to the great recovery in production of the rest of the world. For example, in the first two postwar years, 1946-47, the rest of the world paid for only half of its purchases from the U. S. by receipts from exports to the latter; this was reduced to such an extent that by 1953 the rest of the world paid for about 95 per cent of its purchases from the U. S. All this has also been accompanied by relaxation of discriminatory restrictions against American goods, the terms of trade have improved for the rest of the world, and there has been no serious unemployment anywhere.

This situation has led some to believe that there is no dollar shortage left or that it has virtually been solved. This is true if the sole criterion for judgment is the balance of payments statistics. But if a closer look is taken behind the statistics, it will be found that the problem is far from being solved. For example, the reserves gained by non-dollar countries in 1952-53 are a modest 5 per cent of the transactions of the rest of the world with the U. S., which can be used up in a matter of a few months, as was the case in the year following the outbreak of the Korean war, and thus governments have been reluctant to abolish trade and exchange restrictions while their stocks of gold and dollars are so inadequate. It is also believed that at present we do not have an "easy" balance, that the latter is

greatly dependent on U. S. government purchases of goods and services, which is used mainly for military establishments abroad (offshore purchases). These are very unstable since they are based on international political tensions instead of economic considerations. Another factor influencing this abnormal balance is the fact that much of the world's demand for dollars is forcibly kept down by trade restrictions and exchange controls, which suppresses rather than solves the disequilibrium and forces us to live in a "potential" dollar gap. What is wanted is a long-run balance which is not contrived by the above mentioned artificial means.

It seems that the attempt by some economists to demonstrate that a disequilibrium still exists was made in order to justify continued discussion on much-debated issues and also in order to show the need to analyze the more long-run or secular or underlying causes of the problem. One could actually say that attention at present is concentrated on what Prof. J. H. Williams has called the "longer-run and deeper seated maladjustments in international relationships that go back for at least three-quarters of a century," of which the recent crises have only been symptoms. And thus we get to the main part of this paper which is an analysis of what economists have had to say on the causes of these deep-seated maladjustments.

#### LONG-RUN OR "CHRONIC" CAUSES

*Hicks' Productivity Theory: Background, criticisms, and further developments:* We are concerned with an explanation of the dollar problem by disparities in the rate of increase of productivity in the dollar area and the non-dollar area, causing persistent or ever-recurring pressures. The theory did not originate with Hicks. A direct casual sequence of analyses can be traced through works by Balogh, Haberler and Williams, and, as a matter of fact, Hicks states that he was directly inspired by Prof. Williams' Stamp Lecture. Hicks furnishes a rigorous systematization and elaboration of the theory. It is emphasized that this is a long-run theory because the problem of disparity of economic advance is a long-run phenomenon. Hicks also states that he is not concerned with a balance that might be achieved today, since it is attained with "temporary

expedients"; but what he is looking for are permanent adjustments, and in this respect there has not been a state of equilibrium because disparate increases in productivity occur all the time.

Hicks also makes a few assumptions which should be stated before reviewing his main analysis. He assumes constant cost (all commodities are produced at a cost per unit independent of the amount which is manufactured); this makes it possible to treat all changes in productivity as spontaneous. A distinction is made between "barter" (or real) effects of changes in productivity and monetary effects. Barter effects persist ". . . whatever the course of money incomes—those which remain even if we suppose that money incomes in the various countries can be changed in whatever way is necessary to make adjustments as simple as possible." Monetary effects are those arising out of difficulties in the adjustment of money incomes.

A two-country analysis is presented. It is assumed that productivity in *A* increases more rapidly than in *B*; and so to simplify the whole matter it is assumed that productivity is increasing only in *A*, while remaining constant in *B*. This supposedly makes little difference to the essence of the argument.

Three cases are presented: first, where productivity in *A* increases uniformly, i.e. at the same rate in all industries; second, where productivity increases only in the export industries; and third, where it increases only in import-competing industries. When productivity increases uniformly in *A* the barter effects will usually be favorable to *B*. For example, if money incomes in *B* remain unchanged and increase in *A* by the full rise in productivity, then prices in both countries remain unchanged; since *B*'s incomes remain the same, there will be no increase in what *B* will buy from *A*; but *A*'s demand for *B* exports will certainly rise because its income has risen. In this case the balance of payments will turn in *B*'s favor. But if incomes in *A* rise less than productivity, the balance can remain in equilibrium, and there will also be an improvement in *B*'s real income since *A*'s product can be obtained at a lower price (i.e. *B*'s terms of trade will improve). The monetary effects, however, might not be as pleasing for *B* because *A*'s prices are cheaper and thus more of *A*'s goods will be bought

at the expense of some of *B*'s goods, which will increase incomes in *A* and decrease them in *B*.

The second case is the most favorable to country *B*. Improvements in productivity are concentrated on the export industries of *A*, which means that *B* can get more of *A* goods for the same amount of money. Here it is obvious that we have a real gain for *B*, and monetary troubles are not likely to develop.

And now to the heart of the matter, the case where improvements in productivity are concentrated on the industries of *A* which compete with imports from *B*, i.e. where there is an "import-biased improvement," which results in both real and monetary difficulties. It is assumed that productivity improvements in the 19th century were mainly export-biased, while the opposite holds today. Since this is particularly true in the U. S., it is claimed to be the underlying cause of the continuing dollar problem in Britain and in Europe.

Hicks recognizes that many events have occurred, such as the trouble with war debts in the 1920's, the world depression, the capital flight in the 1930's, the war damage and the present cold war. In spite of all these crises, he believes that:

A special explanation of the difficulties which were being experienced by European countries in settling their dollar debt could always be found. But the continuance of the same consequence, the same dollar shortage, as the result of these various "causes", has by now become very striking. That there is some general influence underlying these particular manifestations can now no longer be doubted. It is hard to see that there is any other general force which would account for what has been happening than the disparity in the growth in productivity. . . .<sup>2</sup>

An important criticism leveled at Hicks is that he accepted his general hypothesis as the central explanation of the dollar problem without presenting evidence to back it up and without considering alternative hypotheses. Of central importance to the hypothesis is that import-competing improvements imply a deterioration of *B*'s terms of trade. But the terms of trade

<sup>2</sup> Hicks, J. R., "An Inaugural Lecture—The Long Run Dollar Problem," *Oxford Economic Papers*, June 1953, 131. For predecessors to the Hicks theory see also: Balogh's *The Dollar Crisis: Causes and Cures* (1950), and Prof. Haberler's analysis in S. E. Harris' *Foreign Economic Policy for the U. S.* in the chapter called "Dollar Shortage?"

turned in Britain's favor in the 1920's and remained thus during most of the 1930's. How then can the dollar shortage in Britain during that period be explained? The adverse monetary effects to country *B* are supposed to be caused by import-competing improvements which imply that money incomes in *A* do not rise as much as the productivity increase. But it is pointed out by critics that money incomes increased faster than productivity in the U. S. during the 1940's and the early 1950's. Thus the monetary effects of the increase in U. S. productivity during and after the war could not be pinpointed as the cause of the dollar shortage in Great Britain at the time. It is also implied that due to import-competing improvements the per capita real income in country *B* will suffer a net decrease, but statistics show that in the past real income per capita has actually increased.

Much criticism is leveled at the assumption that it would make little difference to the essence of the argument if productivity expansion in country *B* is neglected while that in *A* increases. This is why Hicks' analysis leads him to the conclusion that real wages would have to fall in the rest of the world in order to maintain equilibrium with the U. S. (hence his criticism of the 1949 devaluation). But this is practically impossible today because of such institutions as full-employment policies, cost-of-living wage adjustments, and accompanying elasticity of credit supply, which all work against the possibility of a reduction in real wages. One is faced with a dilemma which is best stated by Machlup in form of a question: "How should a nation cope with an 'unavoidable' reduction in per capita real income if it is 'unalterably committed' by its institutions to avoid a reduction in wages?"<sup>3</sup>

Such a dilemma does not arise if real income is either maintained or increasing, and thus there arises a dichotomy in the theoretical model "... between a net loss in real income and merely a retarded increase in real income." It can be shown that the Hicks model in which productivity increases in *A* and remains constant in *B*, cannot be applied to the case where productivity in *B* is also increasing, though at a slower rate than in *A*. Although import-competing improvements in

<sup>3</sup> Machlup, Fritz, "Dollar Shortage and Disparities in Growth of Productivity," *Scottish Journal of Political Economy*, Oct. 1954, p. 262.

this latter case can still produce unfavorable terms of trade for *B*, the effects of this increased productivity in *B* does not have to be nullified by these adverse barter effects. We may thus get an unchanged or increased real income in *B*. There may be a rise in real income even when the terms of trade become less favorable if productivity in *B* increases to a sufficient extent, and as a result, money wages will be able to rise relative to prices while not creating adverse trade and payments conditions "... provided money incomes in *A* have moved up sufficiently to prevent a deflationary pressure on *B*."<sup>4</sup>

Even in the latter case the import-substitutions in *A* have a dampening effect on the increase in real income in *B*. Payments difficulties might result if wage rates in *B* are increased by the full amount of productivity increase since part of the latter has to offset the more adverse terms of trade. A simple inflationary explanation of the shortage could be advanced if money wages in *B* are raised faster than the increase in real income.

Some economists challenge the general assumption that American productivity increases much faster than productivity in the rest of the world. For example, frequent comparisons are made between prewar years (1937 or the average of 1934-38) when the U. S. economy was depressed and the postwar years like 1949 or 1950 when the rest of the world had not fully recovered from the war. Many also ignore the fast growth of the U. S. population, which has risen 25 per cent since 1937, while in the same period the U. K. population rose only by 7 per cent. This is important to keep in mind when comparing increased production figures. It is also claimed that since productivity in the U. S. has increased more rapidly in mining and agriculture, which are predominantly export industries from the point of view of many European countries, as compared to manufacturing, the trend in productivity in the U. S. has not been mainly import-biased. Another criticism leveled against import-biased improvements which are supposed to result in the cheapening of products competing with imports is the fact that in the middle of the dollar crisis of 1946 U. S. prices were rising faster than in other countries. This indicates that relationships are more complex than assumed in theory.

<sup>4</sup> *Ibid.*



A further attempt to throw some cold water on the productivity analysis of the dollar problem has been made recently by MacDougall.<sup>5</sup> He tries to prove statistically that the assumption of productivity in the U. S. rising faster than in other parts of the world has been grossly exaggerated. He shows, using index numbers, that the rate of increase in the production of raw materials, food, and manufactures over the last half century has been about the same in the rest of the world as in the United States. The gain that the U. S. has made over Europe took place mainly during the two periods of war, but in normal peace-time conditions the rates of growth were approximately the same. Unfortunately the output per head of population as a measure of productivity increase does not tell us very much. A better and more meaningful figure would have been the output per person employed in various industries. Some figures comparing annual rates of increase per man-hour worked in manufacturing, agriculture and raw materials also indicate that the U. S. increase has not been much faster than elsewhere. As a matter of fact, some individual countries increased their man-hour output more than the U. S. in peacetime. But most of these statistics are not very revealing since they are aggregates. It is true, however, that they indicate that the differential rates of increase in productivity are not obvious.

We shall devote some attention now to the more positive criticisms of Hicks' model, which in many cases amount to refinements or additions to the original model. Machlup agrees with Hicks that "... it is the import-biased increase in productivity . . . that has unfavorable effects on the country whose exports are adversely affected," but he thinks that the subsequent discussion centers on the *rates* of economic progress, which actually have not much to do with the theory. What is important is the location of the increase in each country. If there is an increase in productivity in both *A* and *B*, but the increase is import-biased in *A* and export-biased in *B*, the terms of trade will turn against *B*. The latter might also lose its competitive advantage in *A*, unless the costs of transportation, handling, and distributing are reduced in the same manner

<sup>5</sup> MacDougall, G. D. A., "Does Productivity Rise Faster in the United States?" *The Review of Economics and Statistics*, May 1956, pp. 155-76.



as the production costs. If productivity increase in *A* is twice as large as in *B*, but is export-biased, while the increase in *B* is uniformly distributed, *B* will benefit. But if the increase is faster in *B*, but export-biased with inelastic foreign demand, and *A*'s improvements are partly import-biased and partly "... in new products for which an eager demand develops in *B* . . .," then the effects will be unfavorable to *B*. All this shows that "... what matters is not a disparity between rates of growth, but the *bias* or *incidence* of particular developments."<sup>6</sup>

At this point the reader might ask himself the following question: does not international trade arise *because* of relative differences in productivity? Why should then a payments problem occur at all? The answer to such a question might lie in the fact that international relationships in the modern world seem to be extremely volatile; and for countries to change in specialization frequently may be very costly, especially to countries not endowed with an abundance of capital and research facilities. And this will be even more severe if it is always the wealthier country which keeps on initiating changes in productivity.

Bernstein also contributes some refinements worth examining. He observes that a general increase in productivity in the U. S. with no increase in other countries will not affect the competitive position of the latter if incomes in the U. S. rise "... promptly in proportion to the increase in productivity." This actually benefits the other countries since a rise in incomes in the U. S. would also mean a rise in demand for imports; and since incomes in other countries have not fallen, there would be no rise in U. S. exports, and thus a deficit would appear on the U. S. balance of payments. This does not happen if incomes in the U. S. rise somewhat less than the productivity increase, so that the increased imports would be balanced by some increased exports. No trouble would arise if productivity increased in the rest of the world, but at a slower rate, and if everywhere incomes rose proportionately. But this is only true if we assume the income elasticity of demand for imports is the same in the other countries as in the U. S. If it is larger in the former, disequilibrium will arise. The cause of this dis-

<sup>6</sup> Machlup, *op. cit.*, pp. 263-5.

equilibrium would then be that American productivity has actually increased in too small a proportion *vis-à-vis* the rest of the world.

In another case Bernstein shows that if improvements in the U. S. are export-biased, improvements in the other countries are concentrated on all but the export industries, wages everywhere rise in proportion to the increased productivity, and productivity increase is greater in the U. S. than in other countries, then the U. S. will become more competitive in third markets because its export costs and prices will tend to fall, while they will tend to rise in other countries (since productivity is increasing in all but the export industries). This does not necessarily lead to adverse balance of payments conditions in the countries affected. Incomes in the U. S. have risen more than in other countries due to increased exports. If the income elasticity of demand in the U. S. is about the same as abroad, increased U. S. imports may well make up the fall in U. S. export prices. Adverse conditions would come into effect if the income elasticity of demand for imports in other countries is substantially higher than in the U. S. because the effect of increased income on U. S. imports "... may not be enough to offset the effects of the stronger price competitive position on U. S. exports."

It should be emphasized that the problems which arise from increases in productivity will not necessarily affect all countries equally. In reality changes in productivity will not be uniformly equal in all industries, and thus other countries will not be affected in similar ways. Where the increase in U. S. productivity not only affects the supply schedule, but also the demand schedule, i.e. where productivity increases involve the appearance of new products, payments difficulties might arise for most other countries because the imports of new goods are not offset enough by reduced imports of older goods to prevent adverse balance effects. Bernstein stresses the need for analyzing productivity changes in the U. S. and their effects in more specific terms in order to see exactly who will suffer.

Some further light was shed on the productivity debate by H. G. Johnson. Increasing U. S. productivity not only affects

<sup>7</sup> Bernstein, E. M., "American Productivity and the Dollar Payments Problem," *The Review of Economics and Statistics*, May 1955, p. 104.

relative prices, but it also raises the real income of Americans and, unless American imports consist of inferior goods, there will result an increased demand for imports. Thus "... increasing American productivity is a factor working against and not towards the emergence of a dollar shortage . . . and could only contribute to the creation of a dollar shortage by increasing too slowly to offset the influence of increasing productivity in the rest of the world on the demand for American exports." Another interesting conclusion of Johnson could almost be regarded as a refutation of Hicks' contention that devaluation will not work. The argument is that the assumption of lower American prices causing the balance of trade to turn in the United States' favor also implies that the international demand elasticities are "... high enough for devaluation against the dollar to improve the trade balance of the rest of the world with the U. S." Decreasing American prices in relation to prices of the rest of the world amount to an appreciation of the non-dollar currencies. If the latter affects the balance of trade of the rest of the world in an adverse manner, it logically follows that a depreciation against the dollar must be effective.<sup>8</sup> Actually this is not a refutation of Hicks, whose main contention was that devaluation does not work because wages respond to price increases.

*Other Explanations of the Problem:* Nurkse views the dollar problem in the framework of theories advanced in his last book.<sup>9</sup> He finds that the gap between America's and the rest of the world's income is very great and is getting wider, while at the same time the world is shrinking in size due to modern communications. All this creates a growing awareness of the "international discrepancies in levels of living." Especially poorer countries are attracted by the high standards of the

<sup>8</sup> Johnson, H. G., "Increasing Productivity, Income-Price Trends and the Trade Balance," *The Economic Journal*, September 1954, pp. 481-2. See also Balogh, T., "The Dollar Crisis Revisited," *Oxford Economic Papers*, September 1954, Vol. 6, No. 3, pp. 243-84; Kindleberger, C. P., "L'asymetrie de la balance des paiements et le probleme du Dollar," *Revue Economique*, Mars 1954, No. 2, pp. 166-89; MacDougall, Donald, "A Lecture on the Dollar Problem," *Economica*, August 1954, NS, Vol. XXI, No. 83, pp. 185-200; Robbins, Lionel, *The Economist in the Twentieth Century*, 1954, pp. 41-59; Sir Dennis H. Robertson, *Britain in the World Economy*, 1954 and Williams, John H., *Trade Not Aid: A Program for World Stability* (The Stamp Memorial Lecture) 1953.

<sup>9</sup> *Problems of Capital Formation in Underdeveloped Countries*, New York, Oxford University Press, 1953.

advanced nations. This results in new wants, a boosted propensity to consume, inflationary pressures and payments problems. Although the orthodox prescription would be for the country to "endeavour to live within its means . . .," it has become socially and politically very difficult, if not impossible, to keep a country within its means when the possibility of higher standards is kept constantly in front of the people's eyes. Nurkse claims that this sets the stage ". . . for a persistent or recurrent tendency to disequilibrium in international trade. . . ." <sup>10</sup>

A main objection to all this would be that it does not satisfactorily explain the problem of Western European countries who are not so backward. The problem is also raised why the "demonstration effect" should be of such importance today when history teaches us that in previous centuries the rich of Europe displayed extravagant living to the humble mass without enticing the latter to copy their examples. A reply to this, of course, is that, coupled with the demonstration of high living standards, the twentieth century also demonstrates the ideal of equal opportunity. But the question still remains as to whether Nurkse hit upon a fundamental and broad enough cause of the dollar problem.

A number of economists are fascinated by prevailing asymmetries in international trade and believe these to be important factors leading to an understanding of the dollar problem. For example, a European depression is not likely to have serious consequences in the U. S., but a minor U. S. recession can easily have major effects on Europe; or both inflations and recessions in industrial countries have magnifying effects on less developed countries; or, for underdeveloped countries the terms of trade improve during inflationary periods and become unfavorable during depressions, whereas the contrary is true for European types of economies. Kindleberger attempts to expose these asymmetries by distinguishing three types of countries: an "adult country" (the U. S.), an underdeveloped country, and a "mature" country (most European economies). The "adult" country is subject to "secular stagnation," while the other two are subject to "secular inflation." The reason

<sup>10</sup> Nurkse, Ragnar, "A New Look at the Dollar Problem and the U. S. Balance of Payments," *Economia Internazionale*, Feb. 1954, pp. 49-51.

for these secular movements stems from the propensities to save and invest in each of these economies. Thus, for example, when there is full employment, savings tend to rise in the U. S. because of the high incomes and because of institutional factors such as the importance of life insurance premiums, and other savings and investment institutions. The tendency to save in underdeveloped countries is low because incomes are low and because the large accumulation of savings, due to maldistribution of incomes, are usually not used for internal investments. In "mature" countries the level of savings is low because of the redistribution of incomes in favor of groups who possess a high propensity to consume and because of the unwillingness of entrepreneurs to reinvest their earnings.

Payments difficulties of underdeveloped countries due to asymmetries are particularly striking. When exports increase, a deficit can be changed to a surplus for only the very short run because this will affect the national income in such a manner that very soon the surplus disappears. This is caused by the high income elasticity of demand for imports in such a country. Ordinarily it would be expected that when the situation is reversed, a surplus in the balance would appear. But the asymmetry prevents this. In underdeveloped countries new goods, which at first are luxuries, become shortly a necessity and the demand becomes quite inelastic when income decreases again.

MacDougall also believes that general international fluctuations have definite tendencies to create a dollar shortage mainly because of these asymmetries. If there exists a surplus in the rest of the world with the U. S., then a small rise in prices in the former can easily restore equilibrium; but if there exists a dollar shortage because of a U. S. surplus, then a fall in the rest of the world's prices will not necessarily restore equilibrium because a rise in import prices will encourage the American import demand curve to move to the left (due to both higher price and encouragement of production of substitutes), and a subsequent fall in price will not restore the demand curve to its old place since ". . . the new technical knowledge acquired will not be lost and the new synthetic factories take a long time to wear out." This does not occur in the opposite direction because most European countries have not the facilities of

building up within a relative short period of time substitute industries.

There are some who contend that monetary influences contributed substantially to the continuing disequilibrium since the war. The fact that the U. S. price level was rising was, according to Robbins, "... a most remarkable stroke of luck. . ." but this was not made use of because there were also inflations in other countries; thus it will never be known what would have happened if U. S. prices had risen while European prices had remained constant or had increased at a slower rate because of the unwillingness of the European countries to restrain their inflation. Robbins actually states point blank that "... the inflations which have actually taken place have been quite enough to account for the disequilibrium on a very substantial scale."

And finally there are some (e.g. Balogh) who are impressed by the strong competitive position of the U. S. They are awed by the high rate of investment activities going on in the U. S. which result in improvements of existing products and new discoveries. The former offers the rest of the world severe price competition and the latter will affect the whole structure of international trade. On top of this, U. S. mass production methods reinforce these aggravating improvements. In addition, superior U. S. marketing techniques, advertising, service organization, and straight price cuts enhance U. S. competitiveness. The latter is made possible by what is called the "intense dynamism" of the system. In such an economy with high investments, inventions cease to be random occurrences but are "reduced to routine activity." This creates monopoly profits which again are used to a great extent for investment and research, and thus we have a vicious circle. It can, however, be questioned whether this dynamism is really so one-sidedly favorable to the U. S.

#### POLICY RECOMMENDATIONS

One of the most interesting discussions of policy measures can be found in Nurkse who examines both tariff and investment measures for solving the disequilibrium. He finds that the American reciprocity trade program of the last twenty years has some basic weaknesses. Under the program the U. S.



made sizable reductions "... only after long and hard bargaining in return for no less sizable cuts by other countries. . . ." But since the other countries had to make sacrifices equal to the U. S., in spite of their dollar deficit, there was nothing left for them but to use quantitative trade and currency controls. Thus, the reciprocity rule in tariff matters resulted in tariff duties being replaced by import controls and inconvertible currencies. Therefore if cuts in U. S. tariff had been unilateral the deficit countries would not have found it necessary to reduce their tariffs and would not have had to institute direct controls. The moral of the story is that reciprocity is based on the assumption of equality in international relations which might be true in the realm of politics, but certainly not in the economic sphere. Although unilateral removal of U. S. tariffs will not be enough to eliminate the dollar problem, Nurkse thinks that it "... would contribute a substantial part of the solution."

Low private U. S. foreign investment in the postwar period is also brought up. An increase "... might not be a substitute for, but at least it would be a good supplement to tariff reductions and increasing American imports." The big difference between investment today and in the last century is that in the latter case both capital and people moved to undeveloped regions, whereas today the flow of capital is a substitute for the movement of people. But in the present undeveloped areas the people are not skilled, they have not grown up in a "capital-minded" milieu, and they "... may not be culturally prepared for the use of Western equipment and technology." Therefore most American investment in the past has consisted mostly of direct American know-how, who operated new installations which assured the companies that the capital would not be swallowed up by consumption. But this promoted "lopsided rather than balanced growth" which was concentrated on raw material production for exports. Investments in capital facilities of these areas and in industries producing for the home market are rare. There has to be found a way for financing public improvements, that is, for constructing a "skeleton framework of overhead facilities" which would encourage investment. Nurkse thinks that investment is not important mainly for the dollars it provides, but rather for remedying



the disparity in productivity ". . . and hence living levels, and so attacking the root of the malady."

This investment remedy is mainly a prescription for underdeveloped areas. Robertson considers the main remedy to be U. S. initiative in controlling her economy, that is, keeping it stable; in evening out her purchasing abroad and thus to prevent specialized countries which depend on U. S. imports from getting into trouble with every slackening of U. S. demand, and in reducing tariffs.

Professor Williams places some of the initiative also on the rest of the world, especially Western Europe. He believes that the basic solution lies in the development of larger trading units which will be able to "cope on more equal terms with the U. S. . . ."; therefore he hopes that Western European integration and the strengthening of the sterling area will soon come about. He also makes some interesting observations on how to conduct increased international investment. Different investment plans for each country are bound to be wasteful and conflicting; thus general planning of investment activities over whole areas might be beneficial.

Both Robbins and Balogh offer the negative solution of discrimination. Although they do not advocate it outright, they both make it clear that a certain amount of it is plausible and should be used (e.g. Robbins shows how a good case could be made by deficit countries to devalue their currencies *vis-à-vis* the U. S. and not between themselves). Balogh believes in discrimination on a "selective basis" in order for the world to cope with the U. S. monster of super production-investment-research activity and sales activity.

#### CONCLUDING REMARKS

It might be useful to use some additional imagination as to the future course of world imbalance. Williams is certainly the most advanced when he envisions the formation of larger trading blocks as a remedy to present problems. In addition to this, the productivity analysts could take some lessons from the theory, so often expounded by Prof. Gerschenkron, which states that there is an advantage of backwardness which provides underdeveloped areas an opportunity to catch up economically with the more advanced nations. The perfect example

in history is Germany's catching up in a few decades with England which had a start of over a century. This is possible because the newly developing countries do not have to go through the experience of the more advanced countries, but can start with the state of present technology; whereas the older countries' advance might be retarded because of obsolete machinery, production methods, etc. Could it not be possible for this to happen to the larger trading blocks which Prof. Williams envisions? By applying comprehensive planning techniques and a coordinated investment policy, it might be possible to catch up sooner or later with the giant across the seas. And this goes also for the more underdeveloped regions of the world. That the U. S. might be burdened by older establishments which hamper modernization is seen by the pressure of interest groups which might retard by many years the replacement of, say, atomic electric plants because of coal or oil interests. If this were true to a certain extent, it would refute Balogh's fatalistic view of the cumulative American giant with which no one can catch up, except by discriminatory tricks.

## POST-WAR FISCAL ISSUES IN CANADA: A CASE STUDY IN THE PROBLEMS OF FEDERAL FINANCE

*J. Stefan Dupré*

### A BRIEF HISTORICAL SURVEY: 1867-1945

IT can perhaps be laid down as a general principle, without inciting any violence on the part of constitutional experts, that no constitution ever turns out in the exact manner that its makers planned. As for a federal constitution which allocates a number of functions to a specific extra layer of regional governments, our principle seems to hold true *a fortiori*.

Canada has certainly been no exception. The men who composed the main part of her written constitution had a considerable background of many years in colonial politics and at the same time could draw lessons from some eighty years of federal experience in a nation that happened to be an immediate neighbor. The latter had great influence on their deliberations. Understandably enough, what most impressed the Fathers of Confederation in the story of American federalism was the bloody Civil War which was taking its terrible toll in lives and property as the very constitutional conferences of Charlottetown and Quebec were in session. Foremost in their minds, therefore, was the need to give the federation which they proposed to found a constitution so engineered that the possibility of such a conflict would be reduced to a minimum. This they did by tipping the scale of power clearly in favor of the central government, and so much so that a noted observer, Professor K. C. Wheare, has probably rightly classified the British North America Act as a "quasi-federal constitution."<sup>1</sup>

By no means did the centralization bias of 1867 overlook the all-important field of government finance. While the Dominion was given power to raise revenue "by any mode or system of taxation"<sup>2</sup> the provinces were restricted to direct taxation.<sup>3</sup> As direct taxation was then thought to include

<sup>1</sup> K. C. Wheare, *Federal Government*, 2nd ed., London: Oxford University Press, 1951, p. 20.

<sup>2</sup> *British North America Act*, Art. 91, sec. 3.

<sup>3</sup> *Ibid.*, Art. 92, sec. 2.

little more than real estate levies, the preponderance given to the Dominion was clear. The provinces were expected to get along on what they could obtain from this source of revenue, to which was added a set schedule of annual unconditional subsidies to be paid by the Dominion and drawn up "in full settlement of all future demands."<sup>4</sup>

The period from 1867 to 1920 was characterized by two aspects: on the one hand a high level of Dominion activity; on the other a gradual vindication of provincial autonomy with decentralizing effects. The Dominion wielded great influence on the national economy by its tariff policy, designed to protect infant industry, and by its credit-worthiness, which enabled it to finance such great projects as the trans-Canada railway. Meanwhile the Judicial Committee of the Privy Council was reviewing a number of legal cases arising from Dominion-provincial questions of jurisdiction, and its decisions clearly extended the limits of provincial authority. Of great importance for provincial finance was the definition of direct taxation adopted by the Court. This being that of John Stuart Mill "a direct tax is one which is demanded from the very person who it is intended or desired should pay it," the door was opened for the provinces ultimately to tax a number of articles merely by making the sellers their agents of collection, and thereby to obtain considerably larger revenue. Also contributing to the increment in provincial revenue was the raising of the annual constitutional Dominion grants. The statutory grants provided for in 1867 had proved inadequate almost from the very beginning<sup>5</sup> and public opinion forced a constitutional amendment in 1907.<sup>6</sup>

The larger provincial income which popular sentiment and the Privy Council made possible in the period 1867-1920 was to stand in good stead during the decade following World War I. Politically divided and saddled with debt, the Dominion Government retired to the sidelines while provincial autonomy reached its apogee. The work to be done lay mostly in the provincial sphere: the motor car necessitated a vast and costly highway construction project while general electrification

<sup>4</sup> *Ibid.*, Art. 118.

<sup>5</sup> Nova Scotia found itself in such dire financial straits in 1869 that it threatened secession—was given a special grant for ten years.

<sup>6</sup> *British North America Act*, 1907.

meant the expense of building power lines and, for the Prairie Provinces, the introduction of a public telephone system. Provincial spending rose from \$90 million in 1921 to \$183 million in 1930, an increment of 103 per cent.<sup>7</sup> This heightened level of spending was not without adverse effects on the poorer provinces. Indeed, the position of the Maritimes became so arduous that a special Commission of Enquiry, the Duncan Commission, had to be formed in 1927 to look into the situation. Subsequently annual emergency grants were paid by the Dominion—\$875,000 to Nova Scotia, \$600,000 to New Brunswick and \$125,000 to Prince Edward Island. The Dominion also had to alleviate a no less precarious situation in the Prairies by giving those provinces control over all their natural resources and by paying them compensatory grants based on revenue which they had not had while their lands were under federal control.<sup>8</sup> But whatever difficulties were suffered in the 'twenties were child's play compared to what was to follow.

The next decade was that of the Great Depression which, needless to say, caused the provincial fiscal roof to cave in. Worse still, the Dominion wanted to balance its budget at any cost. With the per capita gross national product down to \$335 in 1933 from \$623 in 1928 taxes were being increased and the problem of unemployment relief was being tossed from one level of government to another like a hot potato. In general, government spending dropped sharply, and although subsidies to the indigent began to occupy a steadily increasing proportion of expenditure, public investment was allowed to fall with private investment so that virtually no "pump-priming" projects which might have increased employment and stimulated demand took place. At the same time, public debt at all levels of government took on alarming magnitude and the situation of the provinces and municipalities, whose credit possibilities were far more limited than those of the Dominion, reached a critical stage. The rapid increment of taxation on the part of all governments was of virtually no avail; with income and profits at low levels and sharply curtailed demand restricting sales, tax increases were more than offset.

<sup>7</sup> Royal Commission on Dominion-Provincial Relations, 1939, *Report*, Vol. I, p. 150.

<sup>8</sup> *British North America Act*, 1930.

The Dominion did give some aid to the provinces by increasing conditional grants for old age and blind pensions and by making conditional grants for unemployment relief.<sup>9</sup> In addition it loaned some \$175 million to the provincial treasuries much of which was later written off. But these emergency measures proved far from adequate and the poorer provinces fell into particularly unhappy situations. In 1935 the White Commission was created to revise the special grants made to the Maritime Provinces since the days of the Duncan Commission, and these subsidies were forthwith increased. The Bank of Canada in 1937 recommended emergency grants to Manitoba and Saskatchewan. These Prairie Provinces, together with Alberta,<sup>10</sup> probably suffered more from the depression than any other area in Canada. Not only were their important American markets closed to them, but there were continuous droughts, crop pestilence and exorbitant railway freight rates making grain transportation an unbearable expense.

This desperate state of affairs in the West, together with utter financial deterioration in all provinces, led to the appointment of a Royal Commission on Dominion-Provincial Relations on August 14th, 1937. Popularly known as the Rowell-Sirois Commission after its two chairmen, it undertook to make a thorough investigation of all the difficulties arising from the intergovernmental distribution of powers under the constitution and

to express what, in its opinion . . . will best effect a balanced relationship between the financial powers and the obligations and functions of each governing body and conduce to a more efficient, independent and economical discharge of governmental responsibilities in Canada.<sup>11</sup>

A large amount of literature resulted from the work of this commission. Included were submissions by the various governments, special studies by leading experts and finally a *Report* in three volumes. The concluding recommendations were (1) that unemployment relief be made a function of the

<sup>9</sup> The latter averaged approximately \$39 million annually from 1932 to 1939.

<sup>10</sup> This province was so hard hit that it actually went into default.

<sup>11</sup> Royal Commission on Dominion-Provincial Relations, *Report*, Vol. I, p. 10.

Dominion Government; (2) that the power to tax personal income, corporate income, and estates be made an exclusive function of the Dominion; (3) that the Dominion assume provincial debt thereby enabling the provinces to make a clean start; (4) that annual "National Adjustment Grants" be paid to certain provinces<sup>12</sup> to enable these to provide "adequate"<sup>13</sup> welfare service without resort to overly heavy taxation.

The first recommendation, that of exclusive Dominion responsibility for unemployment relief, received immediate attention. On the very day that the Rowell-Sirois Report was presented to Parliament, May 16th, 1940, the Speech from the Throne announced that resolutions would be introduced "for an amendment to the British North America Act which would empower the Parliament of Canada to enact at the present session legislation to establish unemployment insurance on a national scale."<sup>14</sup> The proposal received unanimous support from the provinces, the necessary amendment was passed by the Imperial Parliament in July,<sup>15</sup> and the Dominion enacted an Unemployment Insurance Act in August. This measure was not quite complete as a fulfilment of the Commission's proposals, however, as it left unemployment "assistance"<sup>16</sup> in the hands of the provinces.

To discuss this problem, as well as the Commission's other recommendations a Dominion-Provincial Conference was called for January 14th, 1941. Here, while six of the provinces declared themselves in favor of enacting the Rowell-Sirois plans, the three provinces that were denied "National Adjustment Grants" under the scheme, namely Ontario, British Columbia and Alberta, declined to come to any agreement. It was not unwisely stated by the Premier of Ontario that the measures for which the Royal Commission called were of too crucial a significance to be undertaken with finality at a time when the nation was under the pressure of war.

The Conference did serve a distinct purpose along different

<sup>12</sup> Six. Ontario, British Columbia and Alberta were not included.

<sup>13</sup> The test for adequacy was to be found in the Canadian average.

<sup>14</sup> *House of Commons, Debates*, 1940, p. 6, quoted in A. H. Birch, *Federalism, Finance and Social Legislation*, Oxford: Clarendon Press, 1955, p. 193.

<sup>15</sup> *British North America Act*, 1940.

<sup>16</sup> Relief for those not covered by the Act as "unemployed employables" or in unprotected occupations.



lines. It enabled the then Minister of Finance, J. L. Ilsley, to give advance warning that some tough fiscal days lay ahead. He asserted that the Dominion would shortly have to raise personal and corporate income taxes to a point where there would be virtually no room left for the provinces and that imminent rationing of such items as gasoline and liquor would take a mighty bite out of the provinces' traditional tax revenue on these goods.

In April the same Mr. Ilsley brought down his budget and announced the very measures which he had stated would be necessary. Prime Minister Mackenzie King thereupon wrote to all the provincial premiers asking that their governments surrender all personal and corporate income taxation to the Dominion for the duration of the war and one year thereafter. In return the provinces could choose between receiving *either* the revenues which they had derived from the renounced taxes in the provincial fiscal year ended nearest to December 31, 1940<sup>17</sup> *or* interest payable on provincial debt, less the amount collected from succession duties in the same period of time.<sup>18</sup> In addition, each province was guaranteed annual grants equal to the amount by which its revenue derived in any year from the gasoline tax fell below the amount derived from this source in 1940 and a like subsidy for any decrease in revenue from what had been collected by means of liquor taxes in the twelve months ending June 30th, 1942.

All the provinces signed agreements forthwith and a tightly centralized Canada settled down to the grim business of a war that still had some four years to run. But each agreement stipulated that the Dominion, one year after the return of peace, would "reduce its rate of taxes by such an amount as will enable the province again to use the income tax and corporation tax fields, and in particular . . . (would) . . . undertake to reduce its rate of tax on corporation incomes by at least ten per cent of such income."<sup>19</sup>

<sup>17</sup> This option was the more attractive one for Ontario, Manitoba, Quebec, British Columbia and Alberta as their income tax revenues had been considerable.

<sup>18</sup> This was the more desirable option for Prince Edward Island, Nova Scotia, New Brunswick and Saskatchewan whose income tax revenues were lower than their debt charges.

<sup>19</sup> Dominion-Provincial Agreement: An Act to Authorize and Implement an Agreement between the Dominion and the Province, 5 and 6 Geo. VI, C. 7, 1941-42, p. 20.

## POST-WAR DEVELOPMENTS I: 1945-1950

In the course of World War II, Canada's economy made remarkable progress. From 1939 to 1945 the Gross National Product jumped from \$5,707 million to \$11,850 million in money terms<sup>20</sup> and from \$5,664 million to \$9,315 million in real terms.<sup>21</sup> The percentage of unemployed (as reported by the Trade Unions) fell from 11.6 per cent in 1939 to a negligible 0.7 per cent in the first quarter of 1945.<sup>22</sup> Needless to say, Canada relished this new prosperity after the meager depression years, but a nagging fear existed as to what would happen when peace returned. As in other countries, therefore, when the year 1945 and the proximity of victory dawned, the nation's pulse was beating out a mixed query and ultimatum, "if there was full employment during the war, why not after the war?" Dominion leaders realized the political urgency of the situation and in April 1945 the Ministry of Reconstruction issued a White Paper entitled *Employment and Income*. "The central task of reconstruction," it said, "must be to accomplish a smooth, orderly transition from the economic conditions of war . . . and to maintain a high and stable level of employment and income. The Government adopts this as a *primary object of policy* . . . (and) . . . in setting as its aim a high and stable level of employment and income, *the Government is not selecting a lower target than 'full employment.'*"<sup>23</sup> Thus the Dominion Government was unequivocally accepting responsibility for economic prosperity. And not the least of its problems was that there were nine provincial governments which, by virtue of that oft-vexing form of government known as federalism, would have much bearing on whether or not the transition to a prosperous peace could be made. Little wonder then that the famous White Paper stated, in conclusion, "Permanent and mutually satisfactory financial and administrative arrangements with the provincial governments *are a necessary prelude to full implementation.*"<sup>24</sup>

Accordingly, a Dominion-Provincial Conference was called

<sup>20</sup> *National Income, Accounts and Expenditure, 1926-50*, pp. 26-27, Table 3.

<sup>21</sup> *Ibid.*, pp. 30-31, Table 5. The remarkable degree of price stability was, of course, due to rigid governmental control.

<sup>22</sup> *Canada Year Book*, 1946, p. 751.

<sup>23</sup> *Employment and Income*, April 1945, p. 1. Italics added.

<sup>24</sup> *Ibid.*, p. 23. Italics added.

for August 6, 1945. "The Conference," Prime Minister Mackenzie King stated in his opening speech, "is to be known as the Dominion-Provincial Conference on Reconstruction. Broadly speaking, I should define its purpose as an effort to ensure the maximum of cooperation between the Federal Government and the governments of the provinces, in order that the Canadian people, working together, may achieve the constructive goals of peace as effectively as they have carried on the essential, though inevitably destructive, tasks of war."<sup>25</sup>

Financially speaking, the relative positions of the Dominion and provincial governments was as follows. The former had accumulated a heavy debt during the war and its neck was now firmly wedged into that policy noose entitled "full employment." The latter, on the other hand, had enjoyed five years of high revenue and war-restricted expenditure, and as a result were in a far stronger position than they had been at the end of the depression. Thus the Conference would inevitably consist of (1) requests by the Dominion for a continuation of the war-time tax agreements which concentrated important means of revenue and economic control under its exclusive jurisdiction; (2) suspicion, if not active resistance, on the part of the provinces.

Provincial apprehension was made evident even before the Dominion had the chance to make any proposals. Passages from some of the more striking replies to the Prime Minister's opening speech follow.

*Mr. Drew, Premier of Ontario:* "Many of those who approach the whole problem of government from a strictly business point of view alone are inclined to ignore the very practical considerations founded in history and tradition which makes any merely business approach impossible of acceptance, certainly for many years to come."<sup>26</sup>

*Mr. Duplessis, Premier of Quebec:* "Mr. Prime Minister, I am here today as one of the parents who gave birth to the Federal Government. The Federal Government is the child of the provincial governments; and we hope that the child will never undertake the absorption of the mother."<sup>27</sup>

<sup>25</sup> Dominion-Provincial Conference, 1945. *Submissions and Plenary Conference Discussions*, p. 2.

<sup>26</sup> *Ibid.*, p. 9.

<sup>27</sup> *Ibid.*, p. 20.

*Mr. MacMillan, Premier of Nova Scotia:* "I have noted the remarks made here this morning by the Premier of Quebec and the Premier of Ontario. They are definitely opposed to centralization. Their statements are very welcome, I am sure, to the Maritime Provinces because one of the grievances which the Maritime Provinces have to-day is that there is too much centralization."<sup>28</sup>

Plainly, the Dominion had its work cut out. It brought forth a comprehensive set of proposals covering financial arrangements, social security (including unemployment assistance, old age pensions and a national health plan), public investment policy and transitional measures.

Since the implementation of the proposed programs hinged on the financial question, we shall pause to consider the propositions made under that heading. Briefly, the Dominion wished the provinces to forego personal income taxes, corporate income taxes and succession duties and proposed to pay in return to each government "the sum of \$12 per capita annually, increased or decreased in proportion to the value of the Gross National Production per capita as compared with that of 1941. This proposed annual payment would however be subject to an irreducible minimum equal to \$12 per capita as compared with (the G.N.P.) . . . of 1941."<sup>29</sup>

After much discussion, the Conference adjourned August 10th. It was followed by a series of three meetings in November 1945, January 1946 and March 1946 in which the Prime Minister, three federal ministers and the nine provincial premiers convened as a "Co-ordinating Committee." In the course of these sessions a number of proposals and submissions were discussed, including a complete counter-scheme to the Dominion plan presented by the Province of Ontario. The Dominion Government subsequently decided to modify its propositions, and a second plenary conference was opened on April 29th, 1946 to undertake a final debate of the entire matter.

Summarily, the revised Dominion proposals<sup>30</sup> offered, in exchange for the same provincial tax fields, a new minimum of \$15 per head based on the population of each province in 1942 (or 1941, whichever was greater), this minimum in no case to be

<sup>28</sup> *Ibid.*, p. 22.

<sup>29</sup> *Ibid.*, p. 115.

<sup>30</sup> For more complete details, see below, Appendix "A."

less than 150 per cent of the annual payments made to the provinces under the War-time Tax Agreements (excluding gasoline tax guarantee payments) or less than two million dollars.<sup>31</sup> In addition the Dominion would make a number of conditional grants on an annual basis for such provincial undertakings as general public health, tuberculosis treatments, mental health, venereal disease control, the training of crippled children, professional training and research in public health and the care of blind civilians.

The Province of Manitoba was alone to show any real enthusiasm about the Dominion offer. Ontario, the wealthiest province, maintained a cold and aloof attitude, its Premier Mr. Drew being of the opinion that the Dominion had not paid sufficient attention to his own proposals. Mr. Duplessis of Quebec was completely uncompromising and insisted that provincial rights were being jeopardized; "if the Ottawa proposals are in the nature of take it or leave it, I will leave it and take my train back to Quebec."<sup>32</sup> The remaining provinces, while not opposed in principle, had much to say for their need of obtaining larger pieces of the fiscal pie. The Conference adjourned May 3, *sine die*.

One month later the Dominion Minister of Finance, Mr. Ilsley, brought down his new budget. Therein he made an offer on behalf of the Government, to enter into tax rental agreements with any individual province that might wish to do so. In response to the desires which many provincial premiers had expressed in the closing days of the Conference, the new offer was made somewhat more liberal. Quebec and Ontario, of course, stood pat on their attitudes of rejection while the remaining provinces showed varying degrees of willingness or reluctance. The Dominion had to act fast as the War-time Tax Agreements were about to expire. It further revised its concessions<sup>33</sup> and on the basis of these the four Western and the three Maritime Provinces signed agreements for a period of five years.

The seven provinces that did agree to rent their tax fields

<sup>31</sup> The two million dollars concerned only Prince Edward Island, the smallest province.

<sup>32</sup> Dominion-Provincial Conference 1945, *op. cit.*, p. 531.

<sup>33</sup> See below, Appendix "B."

did so through no great love of the Federal Government or of the centralization involved, but rather purely for revenue reasons. It was a matter of plain arithmetic for them to see that whatever they would have collected from their own income taxes and succession duties, offset by the administrative expenses of such collection, would not have been sufficient to exceed the amount of the rental grants which the Dominion proffered. Ontario, on the other hand, being Canada's most highly industrialized and wealthiest province, knew that its tax potentials were considerable and thus was not willing to give Ottawa anything unless the terms involved would be exactly what it wanted. And Quebec's rejection was based purely on a deep and age-old distrust of centralization based on its racial and religious differences; indeed, the tax revenues accruing to its treasury were less than what the agreement grants would have yielded.

Considering the Dominion's failure to negotiate acceptable terms with the two large central provinces, the Taxation Agreements fell far short of achieving anything close to what had been hoped. In accordance with its promise of 1941 to reduce taxes sufficiently to enable the provinces to re-enter the income and succession fields, the Dominion cut corporation taxes from 40 per cent to 30 per cent from January 1st 1947 and, so that a discriminatory burden would not be placed on corporations in the non-agreeing provinces, the Dominion collected an extra tax of 5 per cent on corporations within the agreeing provinces, turning the proceeds over to these provinces. Thus the 7 per cent corporate income tax levied by Ontario and Quebec did not place firms in these provinces at too serious a disadvantage relative to their competitors elsewhere. Federal succession duties were doubled, but Quebec and Ontario were allowed to impose fully creditable succession duties up to 50 per cent of the Dominion total, and did so. Personal income taxes were cut, and taxpayers in either of the non-agreeing provinces were allowed a credit of up to 5 per cent should these provinces levy their own tax. Quebec and Ontario did not choose to do this, however, restricting themselves to the corporation and succession fields. The two provinces thus showed appreciable moderation, which later caused Mr. Ilsley's successor to the



federal finance minister's portfolio, D. C. Abbott, to "pay tribute to general restraint and reasonableness."<sup>34</sup>

But the Dominion did suffer some loss of revenue and dropped both the Social Security and Public Investment programs that had been proposed at the 1945 conference. In the matter of cyclical control, the post-war stagnation which had been the fear of so many never materialized, so that it is difficult to estimate if Ottawa was seriously impeded in implementing fiscal policy. More will be said about this matter in the conclusion.

Other developments to 1950 deserve mention to complete the picture drawn in this section. Newfoundland became a Canadian province in 1949. Among the financial arrangements were provisions for the usual statutory grants and for "transitional" grants of some \$42 million. The latter, a special device to help the new province raise its standard of living to a level commensurate with the rest of Canada, were to be spread over a period of twelve years. In addition, the Dominion assumed most of the provincial debt, and allowed Newfoundland to retain a surplus that it had accumulated during the war. This surplus, amounting to approximately \$40 million, was to be spent on development projects. As to taxation, a three year agreement, effective from 1949 to 1951, similar to those made with other provinces, was concluded.

In 1948 and 1949, a number of federal grants to all the provinces were implemented. An important series of health grants, extending over a period of five years, was announced and covered such matters as hospital construction, tuberculosis control, public health, mental health, etc. The grants were largely unconditional with the exception of those for hospital construction. The latter were given on condition that the provincial contribution match or exceed the grant and that in no case the Dominion contribution exceed one-third the cost of building any given hospital.

Another major grant program involved the Trans-Canada Highway. Started as a "make-work" project during the depression, it had been allowed to languish during the war. In 1949 the Dominion offered to contribute up to 50 per cent of the

<sup>34</sup> Federal-Provincial Conference, 1950, *Proceedings*, p. 139.



cost of completing the highway, provided that the provinces agree to uniform specifications as to its width and quality. All the provinces with the exception of Quebec agreed to the project. The latter refused to cooperate for a number of reasons that included finance, autonomy, provincial rights and myriad other points. The particularly stand-offish attitude which Quebec displayed in this case was to set the tone for the next four or five years.

#### POST-WAR DEVELOPMENTS II: 1950-1955

On December 7, 1949, Prime Minister Louis St. Laurent addressed a letter to the premiers of all the provinces inviting them to a conference in the fall of 1950. A very eventful period intervened between this time and the day the Conference finally opened.

June 1950 brought war in Korea. The outbreak of hostilities was followed, in Canada as in the United States, by a considerable price inflation. At the same time it became evident that the Federal Government, by a sharply increased defense program, would add further to the flow of expenditure and might thereby aggravate the inflationary trend. The Federal-Provincial Conference<sup>35</sup> was postponed from the fall until December to make way for the presentation of an emergency budget to Parliament. Here, Finance Minister Abbott called for further funds for defense and correspondingly imposed new excise taxes on a number of commodities and, more important still, raised the corporation income tax to 38 per cent. On the political side, there was talk of the possibility of all-out war and, by the time December 4th, the revised day for the Conference, dawned, the general consensus of opinion was that grim days lay ahead.

The inter-governmental correspondence which preceded the Conference had set two main topics on the agenda: (1) fiscal matters, (2) social security with special reference to old-age pensions.

The Prime Minister opened the Conference by presenting, in turn, Hon. Lester B. Pearson, Secretary of State for Ex-

<sup>35</sup> Note the change in terminology from "Dominion-Provincial" to "Federal-Provincial." To maintain conformity with terms used in official documents, this paper will hitherto refer to "Federal" where, in the first two sections it used "Dominion."

ternal Affairs, Hon. Brooke Claxton, Minister of Defense, and Hon. D. C. Abbott, Minister of Finance. Taken together, the speeches of these three gentlemen can be summarized as stating (1) that the international situation was perilous and demanded serious action; (2) that increased defense requirements would incur heavy expenses to the Federal Government, (3) that since federal expenditure would accordingly have to be raised up to the vicinity of "25 per cent of the gross national production,"<sup>36</sup> and this in a highly inflationary period, provincial governments should consequently keep their own spending to a minimum.

The provincial premiers all began by expressing their realization of the critical situation which the country faced, and their willingness to cooperate. But some provinces, notably Newfoundland, expressed doubt that they would be able to do very much about restricting expenditure. The position of Canada's newest province was particularly difficult, as, in the words of its own Premier, Mr. Joseph Smallwood, "Newfoundland entered the Canadian union a backward country"<sup>37</sup> and therefore would find it extremely arduous to cut down spending which had as its only purpose the raising of public welfare to a bare minimum in relation to the rest of the country.

Concerning the first matter on the agenda, that of fiscal problems, Ontario and Quebec again showed grave doubts about the feasibility of tax rental agreements. The Premier of the latter was especially intransigent. "We cannot repeat too often that Confederation is not only the result of an agreement between four pioneer provinces, but that it was based, essentially and fundamentally, *on a convention or agreement between two great races*."<sup>38</sup> This specific raising of the racial issue, as we shall see later, was to assume increasing importance in the following years. The Premier of Ontario, meanwhile, pleaded for "frank recognition that there must be a joint occupation of these (taxation) fields and with this recognition an active spirit of cooperation between the provincial and federal governments."<sup>39</sup>

The other eight provinces, all of which had now had experi-

<sup>36</sup> Federal-Provincial Conference, 1950, *Proceedings*, p. 17.

<sup>37</sup> *Ibid.*, p. 56.

<sup>38</sup> *Ibid.*, p. 26. Italics added.

<sup>39</sup> *Ibid.*, p. 22.

ence with peacetime tax rentals, expressed varying degrees of satisfaction and dissatisfaction. The most common complaint was that the agreements yielded insufficient revenue which was not commensurate to provincial tax potential or need although the Premier of Nova Scotia went further to attack the principle involved. "I do not think that subsidies are the way to settle this problem. I repeat now what I have repeated so often before, namely, that the ideal condition would be to divide the responsibilities of governments and to arm each jurisdiction with the necessary sources of revenue to enable it to carry out its own responsibilities."<sup>40</sup>

Concerning the second topic on the agenda, that of old-age security, the Federal Government proposed (1) to undertake an old-age "pension" plan providing \$40 per month to all Canadians of the age of 70 and up regardless of means; (2) to foot 50 per cent of the cost of provincial old-age "assistance" which would provide monthly sums for persons between the ages of 65 and 70 who met a means test.

Substantial agreement was found on the question of old-age "pensions." But the poorer provinces, notably Newfoundland, showed misgivings about footing the cost which the old-age "assistance" scheme would involve. Apparently, however, the difficulties of this situation were partially ironed out when the Conference retired in committee.

The Federal-Provincial Conference of 1950 adjourned on December 7th. During the *in camera* sessions, Finance Minister Abbott presented concrete federal proposals for possible tax agreements in 1952<sup>41</sup> and the provincial premiers took these home for further deliberation. The Department of Justice was charged with the task of drafting a constitutional amendment which would give the Federal Government authority over old-age pensions.

Action on the proposals for old-age security developed rapidly after the Conference. By the middle of 1951, all the provincial legislatures had consented to propose to the Imperial Parliament an amendment to the British North America Act. The Federal Government submitted the amendment to Westminster forthwith and received immediate approval.<sup>42</sup> The

<sup>40</sup> *Ibid.*, p. 29.

<sup>41</sup> See below, Appendix "C."

<sup>42</sup> *British North America Act*, 1951.

universal \$40 per month pension became law with the Old Age Security Act of 1952. As to old-age "assistance" for those between the ages of 65 and 70 who were without means, agreement was reached with nine provinces for a half-and-half shared cost of providing pensions of \$40 per month, and with Newfoundland on a like basis for pensions of \$30 per month.

The Tax Agreements of 1947 being due to expire in 1952, the matter of fiscal arrangements was taken up in private negotiation between the Federal Government and individual provinces. Although no records are available, it is reasonable to suppose that the talks were mainly characterized by ever more haggling for larger federal rental grants. Indeed, a number of minor alterations were made by Ottawa including one that might have important long run effects: it was promised that, should the 1952 agreements expire without renewal, tax credits would be permitted on provincial income taxes for a period of five years.

But the really big change wrought by the 1952 negotiations was that Ontario joined the fold of agreeing provinces. Since Ontario's about-face was made after private talks with federal officials, it is difficult to put one's finger on the factors that may have stood behind this change of heart. Among these may have been (1) the urge to "try anything once"; (2) the likelihood of prosperous years ahead with accordingly increasing Gross National Products providing larger grant returns; (3) the good will to be gained from lifting the burdens of double taxation from the shoulders of resident corporations. At the Federal-Provincial Conference of 1955, Ontario's Premier Frost was to state, "We entered into the arrangement in 1952 not because it was altogether fair or realistic but because it was the best one that we could make at that time. . . . We regarded the agreement as designed to meet a temporary condition."<sup>48</sup>

By October 29th, 1952, the last agreement had been signed and Quebec remained the lone province outside the fold. The fact that nine provinces had seen fit to rent their tax fields but that one remained completely adamant had a shaping influence on all discussions of federal-provincial relations for the next three years. To a large segment of the public and press outside Quebec, such conduct on the part of only one member

<sup>48</sup> Federal-Provincial Conference, 1955, *Proceedings*, p. 20.

of the Canadian union came to be pictured as an instance of supreme arrogance. And the fact that Quebec is predominantly French brought a number of the old skeletons out of Canada's closet. Premier Duplessis' 1950 Conference statement that Confederation had been a merger of two races as well as of colonies became a prime bone of contention. The Government of Quebec, meantime, felt hemmed in on all sides. With Ontario a party to the tax agreements, Quebec remained the lone province levying a 7 per cent corporation tax, and a newly instituted federal tax credit of but 5 per cent left a gaping 2 per cent at the margin. As a result, many resident corporations were rumbling about moving their head offices to Ontario. In 1953 the Federal Government covered up for Quebec by extending its credit to cover the provincial tax, but while a potentially critical situation was thereby avoided, the entire "Problem of Quebec" (as many began to label it) had much broader and deeper aspects. The "Problem of Quebec," particularly intense through early 1955, came to embrace a scope that extended far beyond the simple question of renting or not renting tax fields.

Its real intensification began over the question of federal grants to universities. In 1951 the Federal Government, taking up recommendations made by a Royal Commission on Arts and Letters (the Massey Commission), had decided to implement a proposal made in the Commission's report that direct federal grants be made to all Canadian universities.<sup>44</sup>

Although aid to education is constitutionally a provincial field, all the English-speaking provinces were more than happy to see their financially hard-pressed universities benefit from such a windfall. The Quebec Government, however, pouted. The Province has long been justifiably proud of the fact that its inhabitants have fostered an island of French culture in a predominantly Anglo-Saxon country. But Quebec universities themselves felt no qualms about accepting the gifts; their financial position was every bit as precarious as that of their sister institutions in the other provinces. At any rate, the Provincial Government insisted that the first grants (for 1951-52) be made in the name of the Provincial Minister of

<sup>44</sup> The basis for these flat subsidies was to be fifty cents per head of the population in each province to be allocated to each university in accordance with the relationship of its enrollment to total enrollment of all universities within the province.

Finance as well as his federal counterpart. Then when the Federal Government wrote out its second series of checks (1952-53), Quebec ordered its universities to refuse the money. This wrought consternation among these institutions, and the matter became a national controversy. Then the Province decided that it must somehow compensate its schools for their loss of revenue. So Premier Duplessis enacted corresponding grants from the provincial treasury. This eased the pressure on the university problem, but was a sharp double-edged sword: the Province was paying out money, all well and good; but where would funds be found to finance this new expenditure? The solution was found readily enough, but became a major issue of contemporary Canadian politics. The answer, of course, was to impose a tax. But this was to be a personal income tax<sup>46</sup> and the rate averaged in general 15 per cent of the federal tax. This naturally meant that the tax burden would be heavier on Quebecers than on residents of other provinces. Federal law since 1947 did permit a tax credit to provinces not party to taxation agreements, but this was at a maximum of 5 per cent. It appeared, therefore, that Quebec taxpayers would be left holding the bag. However, Premier Duplessis, not to be outdone by circumstances, belligerently announced that the only just policy for the Federal Government to adopt would be to allow the entire amount of the provincial tax to be credited against its own returns.

For Ottawa to comply fully with such a demand would have been politically impossible as a great hue and cry would undoubtedly have been raised by the other nine provinces who would have had their hands tied by the taxation agreements while the lone non-agreeing province fattened its treasury without even having to pay the political price of submitting its inhabitants to a higher level of taxation than the rest of the country. But on the other hand federal officials realized only too bitterly the important role which Quebec plays in national politics. Ottawa cabinet members did not have to be reminded that the cost of losing public support among Quebec voters often amounts to four or more years on the benches of "Her Majesty's Loyal Opposition." And they knew just as well that Mr. Duplessis had, through ten long years of unchal-

<sup>46</sup> The tax was enacted for the years 1954, 1955 and 1956.



lenged political power, so fixed the necessity of "provincial autonomy" in the Quebec mind that blame would fall on them for not allowing the desired tax credit rather than on the Provincial Premier for imposing the tax in the first place. The only possible way out of this politician's nightmare was to negotiate.

Accordingly, Prime Minister St. Laurent invited Premier Duplessis to Ottawa in order to quietly talk the situation over. The latter replied bitterly that he would under no circumstances come to the federal capital, in such tones that it is amply evident that he would have considered such a trip the rough equivalent of going to Canossa. Instead, he proposed that Prime Minister St. Laurent come to Quebec City. The Prime Minister refused with a like implication that such a course would be humiliating. After this tragically amusing *impasse*, which one would really expect only from heads of state, the two leaders finally agreed by October to meet in Montreal, a city apparently considered by both to be sufficiently "neutral." They emerged from a hotel suite after a few hours of conversation and entrained for their respective capitals. Some concessions were made by both men, but chiefly by Mr. St. Laurent who agreed to raise the tax credit to 10 per cent.

On January 14th, 1955, the Prime Minister wrote a letter to all provincial premiers with the exception of Mr. Duplessis, in which he set forth his position in granting the higher credit rates.

We are not yet in a position to propose an alternative to the tax rental agreements which we believe would be generally satisfactory and, as the agreements still have two years to run, we felt that, meanwhile, we should provide a stop-gap arrangement which, without being unfair to the other provinces, would reduce the burden of double taxation placed on many of the income tax-payers in the province of Quebec.<sup>46</sup>

The letter went on to state that any province could terminate its tax agreement if it so wished and revert to raising revenue by means of its own income taxes. As matters turned out, the provinces did not take up the federal offer to break the agreements, and Ottawa proceeded to extend Quebec's credit.

<sup>46</sup> Federal-Provincial Conference, 1955. *Preliminary Meeting*, Appendix "B," p. 61.



Then on March 8th Prime Minister St. Laurent sent another letter<sup>47</sup> to the provincial premiers, including Mr. Duplessis, suggesting that it would be advisable for the leaders of all eleven governments to convene in a preliminary meeting in order to determine the agenda for a full-fledged Conference to be held later in the year. All parties thereupon agreed that the preparatory talks begin in Ottawa on April 26th.

The Preliminary Conference aired one plain fact. The great problem of federal-provincial finance was no longer the "Problem of Quebec." It was the problem of the entire idea and function of the tax rental agreements themselves. No province sought to assail Quebec for its actions; rather the premiers seemed almost sympathetic. This was remarkable at the time to many who, having either written or read a steady stream of editorials condemning Quebec, had expected a real showdown to occur. Premier Duplessis himself seemed to have anticipated abuse when, in his opening statement, he had remarked, "Sometimes I am called upon to read the newspapers from other provinces, and really and truly I do not recognize myself in the picture they make of me. I am certainly not the ogre I am represented to be in certain quarters."<sup>48</sup>

But while no stone was cast against Quebec, the Federal Government fell under a not inconsiderable amount of criticism. The leading critic was Mr. Joseph Smallwood, Premier of Newfoundland. Canada's newest province now had five years of federal experience under its belt, and it had admittedly prospered greatly. But many costs which this prosperity involved fell heavily on the provincial treasury, with the result that little money was left to provide social services at anywhere near a level acceptable to the inhabitants of even the very poor provinces of Prince Edward Island, Nova Scotia and New Brunswick. Said Mr. Smallwood:

We might accept the position that we are second or third class Canadians, and that we will continue to do with less . . . of everything than all the other provinces. We might accept that, Mr. Chairman, but before I shall do that I shall tell you now quite frankly as one who had something to do with the movement to bring Newfoundland into Confederation, I would with great joy

<sup>47</sup> *Ibid.*, Appendix "C," p. 62.

<sup>48</sup> *Ibid.*, p. 23.

spend the rest of my life leading a movement to lead Newfoundland out of Confederation. I do not expect that ever to happen because a solution will be found—it must be found. As one Canadian who fought hard to become one, I do not think that the greatness of Canada lies in perpetuating what has taken place up to now, the enrichment of a couple of the more populous provinces (Ontario and Quebec), to which you might add one that is rapidly becoming rich, great and prosperous, Alberta, and to some extent British Columbia. With respect to the rest of the country you have struggling provinces, under-populated and under-developed.<sup>49</sup>

The impact of such a forceful statement cannot be underestimated. The "have-not" provinces of Prince Edward Island, Nova Scotia, New Brunswick and Saskatchewan had long raised their voices against the relatively poor positions which they occupied. To presently hear the spokesman for a brand-new province not tied to Confederation with the firm links of tradition make such a firm appeal for greater aid would add fuel to their own arguments. Thus the entire veil with which the tax agreements had shielded the difficulties of federal-provincial relations from the eyes of the press and public was cleanly ripped away, revealing no rosy picture.

A press communique issued at the end of the final session, which was held *in camera*, revealed that the main Conference would open in Ottawa on October 3rd, and that the following items would constitute the agenda: (1) Federal-provincial fiscal relations; (2) public investment and natural resources development; (3) the desirability of establishing a Federal-Provincial Continuing Committee; (4) health and welfare services; (5) the timing and scope of such other conferences as might be desired.<sup>50</sup>

The question of federal participation in meeting the cost of relief to unemployed persons not covered by the Unemployment Insurance Act had also been discussed in the closed session. It was agreed that this matter should not wait for the October meeting, but should be referred immediately to a committee of federal-provincial officials who would compile the essential facts, examine the problems involved, and report back to their governments as early as possible. The committee in question convened on June 20th and 21st, after which the provincial representatives brought home for consideration Fed-

<sup>49</sup> *Ibid.*, p. 58.

<sup>50</sup> *Ibid.*, Appendix "D," p. 63.

eral proposals that the central government take on one-half the cost of relief for the number of people in need of assistance in any province in excess of 0.45 per cent of the population of that province. The matter has since been taken up only in private talks between the individual provincial premiers and the Prime Minister. So far as is known at the time this paper is being written, certain of the provinces have indicated their approval.

The full-fledged Federal-Provincial Conference of 1955 was duly opened on October 3rd. On the question of fiscal relations, it was apparent from the beginning that, should any new tax agreements be made in 1957, Ontario would definitely not care to participate. This is clear from a statement made by its Premier, Mr. Frost, to the extent that provincial tax credits amounting to a minimum of 15 per cent of the federal tax would alone be realistic. Quebec once again reiterated its position as opposed in principle to any tax rentals whatsoever. British Columbia unequivocally declared that it would not renew any agreement unless much larger allowances were made. Alberta, meanwhile, came up with a proposition for a "joint federal-provincial tax" levied both on individuals and corporations in the form of personal income tax and corporation tax.<sup>51</sup> While the four wealthy provinces could afford to be independent in their outlook, the six "have-not" provinces all appeared resigned to a renewal of the tax agreements. All, with the exception of Manitoba, manifested great distaste for the rental scheme, seemingly accepting only because of financial necessity.

Remaining matters on the agenda received some discussion in the open meeting, and were thoroughly aired *in camera*.

At the conclusion of the Conference on October 7th, a press communique<sup>52</sup> was issued summarizing all the steps made in both the public and closed sessions. As to fiscal matters no definite proposals were made by the Federal Government. The Prime Minister made suggestions concerning a system of equalization payments to be made unconditionally by Ottawa to those provinces whose tax potentials in the fields of personal income taxes, corporation taxes, and succession duties were

<sup>51</sup> This proposal deserves consideration, and is reviewed in the final section of this paper.

<sup>52</sup> *Ibid.*, Appendix "F."

below some defined level. Each province would be free to decide whether or not it wished to enter into a tax rental agreement. It is understood that this proposal met with a certain degree of approval from Premier Duplessis of Quebec. A number of problems and suggestions were brought up in the field of public investment, and it was agreed that a meeting be held at some future date to consider what steps should be taken to continue work on the Trans-Canada Highway.<sup>53</sup> A special committee was appointed to give more detailed consideration to propositions for a National Health Plan.

Finally the Conference yielded a brand new innovation: it was agreed to establish a permanent committee of federal and provincial officials which would meet from time to time to exchange information and examine technical problems in the field of fiscal and economic relations. This may be a step forward. Although the committee cannot take significant action on its own, it might perhaps have value as a medium for the exchange of ideas and opinions, something which in many ways has long been sorely needed.

After leaving Ottawa, the premiers did not return until March of 1956 when a further closed session was held to discuss the basis for possible tax agreements in the future. The mission was a fruitless one, so *Time Magazine* reported in its usual style:

Ten provincial premiers braved one of the winter's worst blizzards . . . to travel to Ottawa and bid for bigger shares of the federal government's tax revenues. It was hardly worth the effort. Finance Minister Walter Harris<sup>54</sup> doggedly refused to increase the grants already offered; the conference, originally expected to last two days, was all over within a few hours after the premiers' storm-delayed trains and planes arrived in the capital. As could be expected, none of the premiers was happy about the fruitless mission. Ontario's Leslie Frost grumbled that the present formula of federal grants was 'archaic.' Quebec's Maurice Duplessis complained that Ottawa was giving the provinces only 'partial restitution.' British Columbia's W. A. C. Bennett charged that the provinces had been deprived of their 'constitutional rights.' Their protests got the premiers nowhere. As they quit the capital, Prime Minister Louis

<sup>53</sup> The present system of federal grants for this project will expire at the end of 1956.

<sup>54</sup> Walter Harris succeeded D. C. Abbott as Finance Minister in 1954.

St. Laurent announced with unconcealed finality that no further federal-provincial conferences were planned.<sup>55</sup>

Little other information has yet been made available as these words are being written. Newspaper comments have carried quotations from a speech by Premier Leslie Frost to Ontario's Legislative Assembly. He claimed that the plan presently offered "completely ignores the plight and needs of municipalities and provinces," and "instead of making provinces . . . strong it is putting them in a position where they will have trouble getting along."<sup>56</sup>

On the basis of present antagonism then, it appears doubtful if any provinces with the possible exception of the poorer ones, will be willing to have any more to do with tax rentals. This would leave as a practicable alternative the scheme of "equalization payments" mentioned in the 1955 Conference's final press communique. What will be done on this score, or on any other for that matter, remains to be seen.

#### A DIGRESSION: THE UNITED STATES AND AUSTRALIA

The survey which has been made in the preceding sections should bring forth an obvious fact: there is very little that Canadians have not tried at one time or another in the matter of federal finance. The period from Confederation until 1941 wrought experience with numerous methods: statutory grants, unconditional "special" grants based on fiscal need, conditional grants for specific purposes, overlapping taxation, etc. World War II ushered in uniform taxation in the income and later the succession fields. Post-war developments continued the tax rental idea with the new device of tax credits for non-agreeing provinces. And presently a scheme of "equalization" payments based on the principles of fiscal equity and tax potential is being mentioned.

But it would not be out of place at this juncture to turn from Canada's background, wide and varied though it is, and to cast an eye in the direction of some other Federal States in order to review just how they have attempted to handle their own revenue-expenditure problems. We shall thus glance

<sup>55</sup> *Time Magazine* (Canadian Edition), March 19, 1956, p. 36.

<sup>56</sup> *Montreal Gazette*, March 21, 1956.

quickly at the United States and Australia, limiting ourselves to these two countries chiefly on account of space limits, and also because certain similarities, e.g. colonial origin, highly diversified economies and wide areas make their experiences particularly relevant to Canada.

The tax powers of the American states are wider than those of the Canadian provinces extending to nearly all forms<sup>87</sup> of taxation, direct and indirect, and in general limited only by the very basic barriers that a federal union must impose on its members if it is to function at all effectively. The three big direct taxes, i.e. the personal income tax, the corporation income tax and death taxes (inheritance or estate taxes to use the American terminology) are all widely imposed. Twenty-nine states and the District of Columbia collect personal income taxes, thirty-two states have a corporation tax, and all states with the exception of Nevada impose a death tax.

Only in the field of death taxes is it possible to credit the state tax against the federal. Here, arrangements have been made whereby the Federal Government permits state taxes to be credited up to 80 per cent of the total federal levy based on 1926 rates. Federal death-tax rates have since been considerably increased, of course, so that the average credit is presently down to the vicinity of 11 per cent.

For personal and corporation income taxes, a complicated system of tax deductibility<sup>88</sup> is used. In the majority of states imposing these taxes, the federal and state taxes are mutually deductible from the tax base; in ten states, including New York and California, the state tax is deductible in calculating the federal tax but deduction of federal income taxes is not permitted in determining tax liability to the state. (This is because state tax deduction is permitted in all cases by federal law, while deduction of the federal tax is contingent on state law.)

The two deductibility systems, and the tax credit method in force in Canada, all have appreciably different effects on the taxpayer's bill. This would be best illustrated by a mathematical example.

<sup>87</sup> Some states, of course, have their own constitutional limitations.

<sup>88</sup> Tax *deductibility* means that tax due to one level of government is subtracted from the *base* from which taxes due to the other level are calculated; tax *credit* that taxes due to one level of government are simply subtracted from the other government's tax *bill*.



Let us assume that the effective federal rate on a taxable income<sup>60</sup> of \$4,000 is 40 per cent and the state equivalent is 6 per cent. If neither deductibility nor a credit is permitted, the taxpayer simply pays \$1,600 to the Federal Government and \$240 to the state, a total of \$1,840.

In the American system *either* (1) the state tax is deductible in calculating the federal tax *or* (2) each tax is deductible in calculating the other. Under (1) the citizen with a taxable income of \$4,000 would still pay \$240 to his state but only \$1,504 to the Federal Government, a total of \$1,744. Under (2) the same income would mean a \$1,541 federal tax and a \$148 state tax, a total of only \$1,689.<sup>60</sup>

With the tax credit system the entire state tax of \$240 would be subtracted from the federal tax bill, leaving an over-all bill of just \$1,600, the same as if only the Federal Government levied an income tax.

From the above, the distinction between the United States and Canada should be amply clear. With the above fictitious taxable income and rates, American Citizen X living in State A which has no income tax faces a payment of \$1,600; Citizen Y living in State B where the state tax is deductible from the federal tax, but not vice-versa must pay \$1,744, and Citizen C living in State Z where there is mutual deductibility pays \$1,689. On the other hand, a Canadian living in any one of the nine "tax-rental" provinces will pay \$1,600; a Quebecer would<sup>61</sup> also pay the same amount even though his province has its own tax.

Overlapping taxation is thus a distinguishing characteristic of federal finance in the U. S. And lack of uniformity is further intensified by different state rates and by the fact that many an individual lives in one state and conducts business in another. Although this constant duplication is the subject of

<sup>60</sup> I.e., income after exemptions and deductions.

<sup>60</sup> Mutual deductibility is calculated by solving the following set of simultaneous equations:  $X_1 = X - xY_1$  where  $X_1$  is the corrected federal tax,  $Y_1$  the corrected state tax,  $x$  the federal tax rate,  $y$  the state tax rate,  $X$  and  $Y$  the gross federal and state taxes. In solving,  $X$ ,  $Y$ ,  $x$  and  $y$  are the "known" factors.

<sup>61</sup> Of course the present Quebec rate amounts to some 15 per cent of the federal tax with a tax credit of only 10 per cent which means that Quebecers pay more than their fellow-Canadians. However, Quebec's presently enacted tax expires in 1956 and it is highly probable that either an extended federal credit will be negotiated or that the new legislation will reduce the rates.

Note: As this manuscript is being prepared for press, a crushing Electoral Victory on the part of Premier Duplessis' National Union Party would seem to indicate that the former is the more probable eventuality.



much complaining and wrangling, it appears to be firmly lodged in the American financial system. Fortunately some steps toward better coordination have been taken, notably in administration where, for example, federal tax returns have been made available to state tax officials and a number of simplifying procedures have been tried out. Among proposals for the future, both federal collection of taxes, eliminating the cost of state tax administration, and the tax credit have been considered. But each method has been met with some impressive objections. Against the former it has been said that there is danger of too much centralization, that problems of distribution are involved, and that past experience in another Federal State, Germany, indicates that federal collection led to extravagance on the part of the state in good times and to insufficient revenue in periods of depression. Against the latter it is argued that a tax credit would limit the power of states to raise taxes as any increment of rates going beyond the amount of the credit would bring immediate dissatisfaction on the part of taxpayers and that present experience with the tax credit in the field of death taxes indicates that the amount of the credit would almost inevitably be too small to be feasible. Thus little improvement seems likely, at least in the foreseeable future. Indeed, it is interesting to note that a number of papers recently presented by a group of distinguished economists, businessmen and bankers to the Joint Committee on the Economic Report give no sign of any significant degree of dissatisfaction. One distinguished economist, Paul A. Samuelson, stated flatly that "the existing structure of federal, state and local taxes is highly satisfactory."<sup>62</sup>

Turning now from the question of taxation to that of grants, the most apparent fact is that the United States has never had a system of unconditional general grants as Canada has. Grants from Washington have rather been for specific purposes and on a conditional, matching basis. They include the National Guard (the lone grant program resulting from a constitutional provision) the Employment Service, public assistance, public health, school lunches, highways, urban development, agriculture and the like. The amount of money annually allotted for

<sup>62</sup> U. S. Congress 84:1, Joint Committee on the Economic Report, *Federal Tax Policy for Economic Growth and Stability*, November 9, 1955, Samuelson, p. 230.

each specific purpose is allocated among the states according to various formulas. The highway grants, for example, take in such factors as state area and population; school lunch grants vary on the basis of population and per capita income. The latter two factors would seem to be particularly satisfactory criteria as they take into account the fiscal capacity of the respective states. On the other hand, one of the most obvious defects of conditional grants made on other bases is that they often allow rich states to attain standards of public services far in excess of the national average while the poorer states, not being able to match the basic conditions, fall far below par.

But all in all, studies on the question of grants seem to indicate in general that the American system of conditional grants is superior to Canada's emphasis on unconditional aid.<sup>63</sup> Indeed the preceding sections in this paper reveal a distinct trend toward American lines: recent aid for old age assistance, highways, public health, etc. has been entirely on a conditional basis.

Numerous proposals have been made in the United States for the improvement of presently existing grant programs.<sup>64</sup> Principal among these are (1) that grants should take into closer consideration the relative degrees of wealth of individual states and (2) that the specific fields covered by the grants should be somewhat broader, restricting areas only to headings of public policy rather than to tiny sub-purposes. Canadians could well afford to take the time to consider these suggestions in formulating their own plans.

Australia in certain ways offers a better comparison to Canada than the United States. The Commonwealth has only six states in contrast with the forty-eight in the American union and the resulting small number of governments makes negotiation procedures, as in Canada, much more feasible. Moreover existing conditions in the individual Australian states offer reasonable comparison to those in the ten Canadian provinces. New South Wales and Victoria, with their relatively high degree of industry and population, can well be likened to Ontario and Quebec; South Australia and Western Australia

<sup>63</sup> The "classic" in this line is J. A. Maxwell, *Federal Subsidies to the Provincial Governments in Canada*, Cambridge, Mass.: Harvard University Press, 1937.

<sup>64</sup> A succinct treatment is found in Arthur Smithies, *The Budgetary Process in the United States*, New York: McGraw-Hill Book Co., 1955, pp. 427-432.

with their heavy dependence on agriculture are in many respects counterparts to Manitoba and Saskatchewan; Tasmania's economic position is somewhat similar to that of the Maritime Provinces, while Queensland has a certain likeness to Alberta and British Columbia in so far as all three are presently realizing their potentialities as possessors of wealth.

The Australian Constitution makes no distinction between direct and indirect taxation. Thus both the Commonwealth and state governments have broad revenue-raising powers although it is definitely allowed that the Commonwealth has financial priority. In the matter of income taxation early coordinating devices made five states the administrators of both federal and state taxes with a sixth state, Western Australia, reversing the process and hiring the Federal Government to administer practically all its sources of revenue. The general defect of this system of joint taxation under uniform administration was, as Commonwealth leaders found out early in World War II, that great difficulty was involved in raising the rate of the federal tax. A committee appointed to report on the problem in February 1942 recommended that the states relinquish the income tax field and that a single federal tax be imposed. The states would be compensated by grants equal to their average income tax revenues for the fiscal years 1939-40 and 1940-41. One and all the states opposed the scheme, but a now famous court ruling<sup>68</sup> declared that it was within the constitutional powers of the Commonwealth.

After the war, an agreement was concluded between the Federal Government and the states whereby the latter accepted a total annual payment of £40 million in exchange for their income tax fields. At first the money was divided among the states in accordance with their previous income tax collections as had been done during the war. However the disparities which this system produced between richer and poorer states made necessary a gradual change whereby Commonwealth money is presently distributed on a per capita basis with due account being taken of the number of residents and school children in sparsely settled areas. This is naturally more satisfactory as it takes into consideration the relative fiscal capacity

<sup>68</sup> *South Australia v. Commonwealth* (1942) 65 C.L.R. 373.

of the several states, but the entire idea of uniform income taxation solely in the hands of the Commonwealth has yet to gain anything approaching widespread approval. A very distinguished economist, Professor Sir Douglas Copland, observed that post-war events have clearly shown that "far from being important agents in the making of economic policy, the states (have) degenerated to the position where they themselves are pressure groups seeking to influence the policies determined by the Commonwealth Government" and indeed that all inter-governmental discussions since the war have been held "in an atmosphere of domination by the Commonwealth and re-crimination by the state, with the worst possible consequences for cooperative administrative action on other points of mutual concern."<sup>66</sup> It also appears that the present over-dependence of the state governments on the Commonwealth has in a number of instances enabled state politicians to pass the buck of political responsibility for their own shortcomings to the Federal Government.

Besides her federal monopoly of income taxation, Australia is distinguished by a large number of federal-state coordination agencies. Among these are the Australian Loan Council, the Commonwealth Grants Commission, the National Works Council and the Agricultural Council, in addition to which there is a number of conferences regularly held at departmental levels which convene the heads of various important ministries.

The Loan Council emerged from a number of financial difficulties that beset Australia in the years following World War I. In the 'twenties a Financial Agreement was concluded between the Commonwealth and the states whereby the per capita grants made to the latter since federation were abolished and the Commonwealth assumed the state debts as of July 1, 1929. The Loan Council was to manage the public debt and control all future borrowings. All seven governments are represented on the Council, the states having each one vote and the Commonwealth two plus a casting vote. The Council has authority over all governmental loans and such related matters as interest rates, maturities, etc. It has thus become a very

<sup>66</sup> Professor Sir Douglas Copland, "The Impact of Federalism on Public Administration," *Federalism: An Australian Jubilee Study*, ed. by Geoffrey Sawer. Melbourne, F. W. Cheshire, 1952, p. 139.

important body in the determination of Australian economic policy. The preponderance of the Federal Government, which needs the concurrence of only two states to carry the vote on any decision, has been widely accepted. But it presently appears that, in addition, Commonwealth control of the Central Bank gives it a virtual veto power over any measure, whatever the stand taken by the states, and while this power has yet to be used, the states have come to resent its possibility with the results that here too complaints of over-centralization are being heard.

The Commonwealth Grants Commission was created in 1933 as a direct result of the Great Depression in order to make reports on applications claiming special financial disability of a state when such arises and thereupon recommends grants for the carrying out of functions which could not be covered by existing state revenues. Functions subsidized thus far have been largely in the range of social services and education.

The National Works Council and the Agricultural Council are less active than the first two organs of coordination. The latter, set up in 1934 and composed of the seven Ministers of Agriculture has as its function the ensuring of Commonwealth-state cooperation along such lines as marketing and agricultural development. Here again, however, the Commonwealth is accused of heavy-handedness, particularly in the area of marketing, where it justifies its action in the light of foreign trade problems and balance of payments difficulties that could arise in the absence of single-minded purposefulness.

The National Works Council played its main role during the war, allocating public work projects among the state according to necessity and priority. Its post-war function has been restricted mostly to making lists of public works planned by the various governments. While the Council could have appreciable significance if it attempted to correlate public projects with varying levels of employment and with the phases of the business cycle, it has shown a marked degree of inertia along these lines, caused largely by the relative stability and prosperity that have characterized Australia's post-war years.

Summing up, it appears that the last two decades have been characterized by a rising preponderance of the Commonwealth Government over those of the states. Whether this trend will

continue in the future may depend largely on public opinion. Recent developments, at least in the academic world, indicate that the centralization of recent years is losing popularity.<sup>67</sup>

#### CONCLUDING REMARKS

Canada's present tax rental agreements are due to expire in 1957. What financial arrangements will then be made is at present anybody's guess. It is doubtful if more than six or seven provinces will be willing to return to the present system. There is a current federal proposal for a return to individual provincial taxes in the personal income, corporation income and succession fields with "equalization" grants to provinces with low tax potentials. Two pressing difficulties can be said to be lurking behind this proposition. First there might well be resentment on the part of many Canadians who have by now become accustomed to the luxury of filling out only one tax form rather than two or more; second, the very poor provinces, especially the Maritimes and Newfoundland, would probably require larger "equalization" payments than the Federal Government could afford or be willing to pay.

These difficulties are derived from a pair of innate characteristics with which federal finance is ever marked. (1) A dilemma between the efficiency of having only one agent for the raising of revenue and the constitutional fact that federalism consists in a territorial division of power and that principles of financial responsibility indicate that the autonomous government that spends money should logically be the one that raises it. (2) The simple arithmetical fact that in any federation of size and diversified economy some areas, and therefore provinces or states, will almost inevitably be poorer, others richer.

While these problems have ever been present in the United States and have been the source of many complaints, that country, unlike Canada and Australia, has yet to be forced to grapple directly with the issues involved. A multiplicity of factors lies behind this fact, among which the great wealth of the nation as a whole and the general attitude of the states and people are undoubtedly the most important. The level of

<sup>67</sup> See for example, the papers in *Federalism: An Australian Jubilee Study*, cited above.



national income is such that both federal and state governments can, without too great difficulty, if not with efficiency, raise sufficient revenue in overlapping fields. Then, the states, partly for historical and partly for social reasons, have always pictured themselves as semi-sovereign units, far more so than the Canadian provinces or the Australian states. Thus not only are the poorer states not insistent on providing social services at a national average level, but, as economist Roy Blough rightly points out, many are even "unwilling."<sup>68</sup> The population, meanwhile, is not overly adverse to duplicate taxation; Dean Erwin Griswold has recently pointed out<sup>69</sup> that the concept of local responsibility is still sufficiently important to the American taxpayer to balance the inconvenience and expense which it costs him.

It appears, then, that the American system could not very well be adapted to the present situation in Canada. And Australia, we have seen, has succeeded in centralizing federal finance to an appreciable degree. It should be amply evident from our description of post-war developments that the Canadian provinces and their people just will not accept that much centralization; indeed Australians themselves are becoming somewhat disillusioned with it.

Canada's "dream" system of intergovernmental financial relations would have to include enough centralization (1) to ensure the carrying out of necessary federal functions; (2) to provide the Federal Government with sufficient control to use fiscal policy as an instrument of anti-cyclical regulation; (3) to enable the Federal Government to pay out funds to supplement those provincial treasuries unable to foot the cost of a satisfactory level of social services. At the same time there would have to be sufficient decentralization to make it possible for the provinces to raise all, or most of their revenues by means of their own taxation, but with as little inconvenience to the taxpayers as possible.

The tax rental agreements, criticized though they are today, were instituted for purposes that are certainly worthy enough: to establish a more equitable system of taxation throughout Canada

<sup>68</sup> Roy Blough, "Fiscal Aspects of Federalism," *Federalism, Mature and Emergent*, New York: Doubleday & Co., 1955, p. 389.

<sup>69</sup> *Federalism: An Australian Jubilee Study*, pp. 105-109.



by reducing duplication of direct taxation and machinery for the collection of direct taxes; to give a greater measure of stability to the revenues of the province in order to enable it more adequately to carry out its responsibilities; to enable Canada, with the cooperation of provincial governments to carry out fiscal and other national policies intended to maintain high levels of employment and production.<sup>70</sup>

The great advantage of these agreements, at least as far as economists are concerned, centers around the fiscal policy aim. Indeed, an impressive case in favor of the tax rentals can be built up on this side, for income taxation is an important instrument of anti-cyclical measures. Consumption and investment can be stimulated by reduced levels of taxation in the downswing of the cycle; contrariwise, higher taxes can restrain overly rapid business expansion. While it is admitted that the provinces could be counted on to impose higher taxes thereby helping to control inflation, the warding off of recession by deficit financing is said to be completely impossible at their level. This is true for two reasons: first, provinces do not have the Federal Government's capacity to borrow; second, they have no central bank at their disposal and are constitutionally unable to "create" money. Thus it is maintained that the only conceivable policy for achieving economic efficiency is to concentrate income tax powers in the hands of the Federal Government.

On the other hand, the chief economic bone of contention voiced by nearly all<sup>71</sup> the provinces against the agreements has centered around their second aim, namely stability in provincial revenue. It is maintained that much trouble lies in the fact that revenue is too stable and that this seriously limits provincial capacity to expand social services and development projects when the need for these arises. The rapid concentration of industry in the more prosperous provinces has given rise to great expense in expanding such services as education and health, while the poorer provinces have to make large

<sup>70</sup> Federal-Provincial Conference, 1955. *Proceedings*, p. 15.

<sup>71</sup> This, of course, has nothing to do with Quebec's consistent refusal to join; its reasons are wholly constitutional as tax agreement grants accruing to it would have been higher than its present tax revenues offset by the costs of collection.

outlays on development projects that might have the long-run result of enriching them.

Certainly, both sides have strong arguments in their favor. But the provinces can ultimately back up against something more than the economists, namely their constitutional rights. And despite the righteous manner in which some economists present their side of the case,<sup>72</sup> it is perhaps doubtful just how correct is their analysis of the situation. While economics does have a theoretical case for the reduction of taxation in a recession there is much disagreement as to how large a cut is necessary and, especially where corporations are concerned, useful; an average size tax reduction should not imperil the Federal Government even though it may be sharing a tax field with a province. And it is well to remember that increasing expenditure in the downswing, thereby "priming the pump," can be even more effective than tax reduction.

One possible compromise that has been advanced in the anti-cyclical policy vs. provincial revenue dilemma is rigid delineation of tax fields, the Federal Government taking authority over all direct taxes and the provinces over indirect taxes. Unfortunately such a plan has serious disadvantages in so far as it can lead to discriminatory taxation among the provinces and can be a far greater source of economic inefficiency. The latter arises from the fact that indirect taxation is highly regressive and can thus be far more of an obstacle in recovering from a recession than a high level of progressive direct taxation.

The most reasonable proposal of late was made by Premier E. C. Manning of Alberta at the Conference of 1955.<sup>73</sup> The first part of his scheme is that "federal-provincial" taxes on personal and corporation income be collected by Ottawa, this simply meaning that the Federal Government would act as the collection agency for both its own and the provincial taxes. Second, Mr. Manning's plan proposes that a national average of provincial revenue be computed on the basis of population, per capita income and so on, and that any province whose tax revenue does not come up to the national average be made

<sup>72</sup> An exceptionally good example is Maurice Lamontagne, *Le Fédéralisme Canadien*, Québec: Presses Universitaires Laval, 1954.

<sup>73</sup> *Proceedings*, p. 93.

a recipient of fiscal need subsidies. Now these subsidies would not come from the Federal Government alone *but also from provinces whose revenues exceeded the average*, thereby involving direct transfer payments from the richer to the poorer provinces. By way of comparison, it is very interesting to note that the present German Basic Law makes provision for a like type of direct payments.<sup>74</sup>

Mr. Manning's plan is a little idealistic perhaps, but it does combine the important features of simplicity for the taxpayer, provincial autonomy in the raising of revenue, and equity payments to the poorer provinces. There has independently been an appreciable degree of speculation in the economic world<sup>75</sup> about the feasibility of such a system. Two problems at least are involved: computing a "national average" that will suit both poor and rich provinces, and convincing the rich provinces<sup>76</sup> that some transfer payments should be made to their poorer cousins. The plan at least has the virtue of being a good compromise—and good compromises usually make for good federalism. What is needed most of all is a broad outlook on the part of all provincial leaders; certainly the transfer payments are a means both to a more prosperous Canada and to autonomy in taxation without inefficiency.

If the taxation agreements will not be renewed in 1957, and the attitudes of at least three provinces plus the intransigence of the Federal Government in yielding any better terms both point very strongly to the possibility that they will not, only the months ahead can tell what will replace them. Presently the "equalization payments" plan which Prime Minister St. Laurent broached at the 1955 Conference might offer an alternative. Two very big question-marks here, however, would seem to involve just how these payments can be made big enough without exclusive federal control of the direct tax

<sup>74</sup> Article 106 (4). "In order to ensure the working efficiency even of the Länder with a low tax potential . . . the Federation may make grants and take the funds necessary for this purpose from specific taxes of those accruing to the Länder.

<sup>75</sup> For example: John Buchanan, "Federalism and Fiscal Equity," *American Economic Review*, September, 1950; R. N. Bhargava, "The Theory of Federal Finance," *Economic Journal*, March, 1953; R. Dehem and J. N. Wolfe, "The Principles of Federal Finance and the Canadian Case," *Canadian Journal of Economics and Political Science*, February, 1955.

<sup>76</sup> It is encouraging to note that Mr. Manning is himself premier of one of the wealthier provinces.

fields and, not without importance, just how the electorate outside Quebec will react to losing the now familiar luxury of single tax forms. Of course there is still time to discuss something akin to Mr. Manning's proposal (which unfortunately seems so far to have gotten lost in the shuffle), or for federal tax experts to concoct some brand new scheme. To make any kind of forecast at this moment unfortunately requires more clairvoyance than the author of the present paper possesses. A leading Canadian tax expert, J. Harvey Perry, has stated that in all his years of close contact with federal-provincial negotiation, the main lesson he has learned is that the subject of federal finance "is a compound of a great deal of simple arithmetic, a considerable element of practical politics, and a modicum of pretentious nonsense."<sup>7</sup> We shall close on this note.

#### APPENDIX "A"

Definition of the Specified Annual Payment to Be  
Made by the Dominion to a Province under the  
Proposed Agreement.

1. The Dominion undertakes to pay the Province for the duration of the agreement a guaranteed annual payment equal to Fifteen dollars multiplied by the number of the population of the Province in 1942 . . . (or at the option of the Province the number of the population of 1941. . .). This guaranteed minimum, however, shall in no case be less than 150 per cent of the annual payments made to the Province under the Wartime Tax Agreement (excluding gasoline tax guarantee payments) or less than Two Million dollars.

2. In any year in which the amount arrived at by the following formula exceeds the guaranteed minimum, the amount so arrived at shall be paid in lieu of the guaranteed minimum. The formula: Divide the 'Gross National Product per capita' for each of the three preceding years by the 'Gross National Product per capita for 1942'. Multiply the quotient in each case by \$15.00. Multiply the product in each case by the number of the population of the Province for the year in question. . . . Average the three amounts so arrived at. . . .

<sup>7</sup> J. Harvey Perry, "What Price Provincial Autonomy?" *Canadian Journal of Economics and Political Science*, November, 1955, p. 432.

Source: Dominion-Provincial Conference (1945), *Dominion and Provincial Submissions and Plenary Conference Discussions*, P. 390.

Clarification of Number 2:

Calculation of grant payable to Province A for 1947.

GNPpc: Gross National Product per capita.

P/p: Provincial Population in year given for GNP.

$$\frac{1}{3} \left[ \left( \frac{\text{GNPpc } 1944}{\text{GNPpc } 1942} \times \$15 \times P/p \right) + \left( \frac{\text{GNPpc } 1945}{\text{GNPpc } 1942} \times \$15 \times P/p \right) + \left( \frac{\text{GNP } 1946}{\text{GNP } 1942} \times \$15 \times P/p \right) \right]$$

## APPENDIX "B"

The revisions made by the Dominion changed the basis on which guaranteed minimum payments to the provinces were to be calculated. Instead of number 1 in Appendix "A", the provinces could now choose among the following three options.

### First Option:

1. \$12.75 per capita on the 1942 population of the province;
2. 50 per cent of the revenue of the province from personal income and corporation taxation in 1940 as determined for the purposes of the Wartime Tax Agreements; and
3. The statutory subsidies payable to the provinces for the year 1947.

This option was more favorable for all provinces but Nova Scotia, Saskatchewan and Prince Edward Island.

### Second Option:

1. \$15.00 per capita on the 1942 population of the province; and
2. The statutory subsidies payable to the province for the year 1947.

This option was more favorable for Nova Scotia and Saskatchewan, two low tax-potential provinces.

### Third Option:

A flat grant of \$2,100,000.

Of interest only to tiny Prince Edward Island.

Source: A. Milton Moore and J. Harvey Perry, *Financing Canadian Federation*. Tax Paper No. 6, Canadian Tax Foundation, Toronto, 1953.

## APPENDIX "C"

(1) Under the new offer, guaranteed minimum annual payments were to be determined by one or the other of the following options:

*First Option:*

The Guaranteed Annual Payment options of 1947 raised by the ratio of increase in gross national production per capita and provincial population between 1942 and 1948.

*Second Option:*

1. The yield of a personal income tax at 5 per cent of 1948 federal rates applied to 1948 income in the province;
2. The yield of a tax of  $8\frac{1}{2}$  per cent on corporation profits earned in the province in 1948;
3. The average revenue received by the province from succession duties;
4. Statutory subsidies payable to the province for 1948.

*Source:* Federal-Provincial Conference, 1950, *Proceedings*, p. 142.

(2) The complicated formula of 1947 by which payments due to be above the guaranteed minimum were calculated was replaced by a simpler one.

The *adjusted* payment is calculated by increasing the guaranteed minimum annual payment by a ratio, calculated for the single year preceding the year of payment, of the following factors: (1) The gross national product per capita for the single year in relation to 1948; (2) The provincial population for the single year in relation to 1948.

*Example:* Adjusted payments for 1955 would be calculated by means of the following:

$$\text{Minimum payment} \times \frac{\text{GNPpc 1954}}{\text{GNPpc 1948}} \times \frac{\text{P/p 1954}}{\text{P/p 1948}}$$

On the eve of final negotiation, Finance Minister Abbott declared that provinces could choose to have the GNP and population determined on a two-year moving average if they so wished. This would give greater stability.

## PART IV

### TOTALITARIANISM AND DEFENSE





## WAS FASCIST ITALY TOTALITARIAN?

Dante L. Germino<sup>1</sup>

THE question of whether or not Italian Fascism was "totalitarian" has been frequently answered in the negative by students of modern dictatorships and specialists in Italian studies. The Italians themselves, with the rare exceptions of Salvemini and Salvatorelli, have been quick to find affinities between the Fascist regime and mild-mannered despotisms like Salazar's in Portugal. As for non-Italians, three representative citations should suffice to illustrate prevailing scholarly opinion.

Sigmund Neumann has observed: "Italian Fascism, in comparison to national socialism, was a mere prelude to revolution. . . . It never matured into a full-fledged modern dictatorship."<sup>2</sup> In his recent volume on Italy, the historian H. Stuart Hughes has stated flatly that "Although Mussolini . . . coined the word 'totalitarian' to describe his regime, the Duce's Italy, as compared with subsequent development in the Nazi and Soviet states, scarcely deserved that title."<sup>3</sup> Dr. Hannah Arendt has been even more emphatic: Mussolini's regime was "Not totalitarian, but just an ordinary nationalist dictatorship developed logically from a multiparty democracy."<sup>4</sup> Portugal, Spain and the Poland of Pilsudski are, according to Arendt, other examples of nationalist dictatorships.

The writer proposes to examine on the basis of the information now available<sup>5</sup> the validity of these assertions about Italian Fascism. The basic problem of an analysis of this kind is the definition of the word "totalitarianism." Fortunately, a definition has recently been put forward by C. J. Friedrich

<sup>1</sup> The writer wishes to thank the Fulbright Commission for the opportunity to spend a year in Italy studying Fascism. Professor Carl J. Friedrich has given careful attention to the material presented here and has made many helpful suggestions, for which the author is deeply grateful.

<sup>2</sup> See Taylor Cole, ed., *European Political Systems*, New York, 1953, p. 322.

<sup>3</sup> H. Stuart Hughes, *The United States and Italy*, Cambridge, Mass., 1953, pp. 73-74.

<sup>4</sup> Hannah Arendt, *The Origins of Totalitarianism*, New York, 1951, p. 256.

<sup>5</sup> This is not the place to give a bibliography. An extensive one accompanies the author's Ph.D. thesis: *The Italian Fascist Party, 1925-1939* (Harvard University, 1956). The flood of memoir material has added immeasurably to our understanding of the Fascist system. The Italian government, however, will not allow scholars to consult many valuable documents. There was not in Italy, as there was in Germany, mass publication of secret documents concerning the dictatorship.

which promises to clear up much of the confusion normally accompanying the use of this term. As a result of an extensive study of Fascist and Communist dictatorships Friedrich has extracted four characteristic and unique features of totalitarian systems. These traits have the great advantage of being empirically verifiable with respect to any current or recent dictatorship.<sup>6</sup>

The four "factors or aspects which basically are shared by all totalitarian societies of our time" are: (1) "An official ideology . . . characteristically focused in terms of chiliastic claims as to the 'perfect' final society of mankind"; (2) "a single mass party . . . organized in strictly hierarchical . . . manner, usually under a single leader and typically either superior to or commingled with the bureaucratic organization"; (3) a "technologically conditioned near-complete monopoly of control . . . of all means of effective mass communication"; and (4) a "system of terroristic police control . . . directed not only against demonstrable enemies of the regime but against arbitrarily selected classes of the population. . . ." This essay will attempt to apply these criteria to the Fascist system. It should be emphasized, however, that these features do not appear fully developed at the outset in any totalitarian dictatorship. Rather, they constitute a pattern toward which a totalitarian system steadily evolves. Traditionalist dictatorships, on the other hand, lose their totalitarian momentum, stagnate and end by falling far short of the pattern.

#### FASCIST IDEOLOGY

In contrast to the Nazi and Soviet regimes, which as pre-power movements had a long period in which to develop fixed doctrines, Italian Fascism came to power with only the most nebulous concepts to distinguish itself from other political forces. Mussolini himself had written only newspaper articles of a transitory nature and had, prior to the March on Rome, neither the time nor inclination to compose anything compa-

<sup>6</sup> C. J. Friedrich, "The Unique Character of Totalitarian Society," in *Totalitarianism* (Cambridge, Mass., 1954), pp. 47-60. Dr. Arendt, whose basic assumptions on Fascist Italy this article is challenging, seems to be in agreement with the definition (*ibid.*, p. 75). Friedrich actually lists five "traits," but has since dropped one from the "unique" category (weapons monopoly).

<sup>7</sup> *Ibid.*, pp. 52-53.

nable to *Mein Kampf*. Nor was there any venerable oracle resembling Marx which the Fascists regarded as the source of doctrinal truth. The Fascist movement could claim in these three short years no figure like Rosenberg, interested in formulating systematically the new party's ideas.

This peculiar early development of Italian Fascism produced a striking conflict in the area of ideology when Giovanni Gentile, a former disciple of Croce and until early 1923 a member of the Liberal party, was converted to Fascism. Gentile decided to fill the Fascist ideological void by constructing his own political theory of Fascism. Because of his reputation in Italian intellectual circles, his two books of the 'twenties, *Che cosa è il fascismo* (1925) and *Origini e dottrina del fascismo* (1929), came to be regarded by many as the most significant expressions of Fascist ideology. An avowed disciple of Hegel, if not a correct interpreter of him, Gentile developed in these volumes, through the medium of his own brand of historical idealism (called "actual idealism"), the concept of the "ethical state," the actual embodiment of which he curiously found in the dictatorship of Benito Mussolini.

Actually, Gentile's influence on Fascist ideology has been vastly overrated. If ideology in a dictatorship is defined as an idea or combination of related ideas which apparently influences the practical political measures taken by the leaders of the regime and which is promulgated by the party and other organs as the official explanation for these measures,<sup>8</sup> then Gentile cannot be called one of the principal Fascist *idéologues*.<sup>9</sup>

<sup>8</sup> This definition follows closely that given by C. J. Friedrich and Zbigniew Brzezinski in *Totalitarian Dictatorship and Autocracy*, Cambridge, Mass., 1956. A totalitarian ideology is a reasonably coherent body of literate ideas "concerning practical means of how totally to . . . reconstruct a society by force . . . , based upon an all-inclusive . . . criticism of what is wrong with an existing or antecedent society." Ideologies are "essentially action-related systems of ideas."

<sup>9</sup> The party old guard opposed Gentile from the beginning because it regarded him as a late-comer to the game and because it feared an attempt by Gentile to usurp the place of the *Duce* as sole fountain of Fascist wisdom. In 1933, party veteran and extremist G. A. Fanelli published an out-and-out attack on Gentile's ideas under the title of *Contra Gentiles mistificazioni dell'idealismo attuale nella Rivoluzione Fascista*. For a discussion of the opposition to Gentile in party circles see "Gentile e gli antigentiliani," in A. Tamaro, *Venti anni di storia, 1922-1943* (3 vols., Rome, Tiber, 1954), III, 79-81. In much the same way Rosenberg took "the most jealous care to prevent Oswald Spengler, Moeller van den Bruck, or Othmar Spann from gaining any hold on the [Nazi] party. . . ." Karl Paetel, "The Reign of the Black Order," in *The Third Reich* (New York, 1955), p. 643.

It is useful for purposes of analysis to draw a sharp distinction between Italian Fascism's "working ideology" and its "ideology for export." The ideology for export, only tolerated by the regime, spoke of the "ethical state" and a kind of pseudo-democratic corporativism. Foreign scholars who in the 'twenties and 'thirties chose to dwell on this aspect of Fascist thought created a biased picture of what the ruling elite really believed and preached to their followers.<sup>10</sup>

The core of Fascism's working ideology, as it may be gleaned from the most significant speeches of Mussolini and his party cohorts and from the indoctrinating manuals of the party and its youth organizations was neither simple nationalism nor nineteenth century state-worship, but a universalistic paganism modeled after the example of ancient imperial Rome.<sup>11</sup> Italian Fascism was not simply a *coup d'état* of a rightist Nationalist group—of an Italian Hugenberg rather than an Italian quasi-Hitler. It was not from the right wing of the *Risorgimento* that Fascism drew its ideological inspiration.<sup>12</sup>

The Fascist party's "catechism" for the youth organizations explicitly repudiated any theory explaining Fascism in simple nationalistic terms.<sup>13</sup> It is true that Mussolini had at first, as Hitler was to do after him, told the world that Fascism was not an article for export. But in a speech of October 23, 1930, *il Duce* denied that he had ever made the statement. Instead,

<sup>10</sup> Dr. Arendt seems to have made the error of interpreting Fascist ideology from the standpoint of the ideology for export when she describes corporativism as "an attempt to solve the antagonism between state and society . . . with a new integrated social organization. . . ." *Origins*, p. 258. As Salvemini, Louis R. Franck, and, most recently and most tendentiously, Ernesto Rossi have shown, corporativism was simply a fancy name for the surveillance of the workers and a rigid system of party-dictated controls over production, prices and trade. Bottai, who along with Ugo Spirito was a leading "corporativist," has described the *fallimento del corporativismo* in his memoirs, *Vent'anni e un giorno* (Rome, Garzanti, 1949). The scores of books and articles written by social scientists in the 'thirties on this "new integrated social organization" obscured these basic facts.

<sup>11</sup> G. A. Borgese, in *Goliath. The March of Fascism* (New York, 1938), properly stresses the call of Rome.

<sup>12</sup> Gentile, on the other hand, preferred to find his intellectual roots in the "near and uncancellable tradition of our *Risorgimento*." He deplored, in a little work called *La tradizione italiana* (Florence, Sansoni, 1936), Fascism's "Roman rhetoric," asserting that "Rome is not the particular tradition of the Italians, but of the Europe which it created."

<sup>13</sup> "Q. Is Fascism exclusively an Italian phenomenon?  
A. Fascism, as far as its ideas, doctrines, and realizations are concerned, is universal . . . it is the sustainer and creator of a new civilization." *Il primo libro del fascista* (Rome, P.N.F., 1942 ed., p. 44).

Fascism was the "order of the day in all countries"; soon there would be *una Europa fascista*. As Fascist or semi-Fascist movements sprang up in Hungary, Romania, Austria, Great Britain, Spain, and Switzerland, Rome was revered as the capital of the European Fascist empire, and Mussolini was kept busy receiving delegations from these countries. In a speech on October 25, 1932, commemorating the tenth anniversary of the "Fascist Revolution," *il Duce* described his regime as a "Third Rome." The twentieth century was to be "the century of Italian power . . . the century during which Italy will return for the third time to be director of human civilization." "Within ten years," he shouted, "Europe will be Fascist or Fascitized! . . . The antitheses which agitate contemporary civilization are capable of resolution only in one way: through the doctrines and wisdom of Rome. . . ."

In his famous article written for *L'Enciclopedia Italiana*, Mussolini called the Fascist regime a "will to power and empire." The Roman tradition, he wrote, "is an idea of force. . . . For Fascism the tendency to empire . . . is a manifestation of vitality, while the opposite is a sign of decadence. . . ." He went on to show how the Roman rhetoric served as a rationale for tightened internal controls and a system of terror. Empire "demands discipline, coordination of forces, duty and sacrifice: this explains many aspects of the regime's practical action, and the necessary severity against those who would oppose themselves to this . . . fateful impulse of twentieth century Italy."<sup>14</sup>

As the core of Fascist ideology, the Roman obsession did indeed "explain many aspects of the regime's practical action." There is little doubt that the Roman madness was the principal motivation behind the Ethiopian dare, the first great break in the European security system of the interwar years and the "prelude to World War II" (Salvemini, in *Mussolini diplomatico*). This stretch of desert was hardly economically or strategically worth the risk of flouting the entire League of Nations. Only in the ideological context does the enterprise make sense.<sup>15</sup>

<sup>14</sup> *La dottrina del fascismo*, Part II, paragraph 13.

<sup>15</sup> Friedrich and Brzezinski, *op. cit.*, distinguish between nineteenth-century imperialism and the imperialism of twentieth-century totalitarian dictatorships. The former was "an outgrowth of the industrial economy," while the latter is related to "the will to conquer the world which animates the totalitarian systems," and is "intimately linked with ideological pre-occupations."

With the initiation of the Ethiopian campaign, the emphasis on Rome in Fascist thought reached such proportions as to exclude all other concepts.<sup>16</sup> In his victory speech of May 9, 1936, Mussolini, to the shouts of thousands upon thousands of jubilant followers, saluted "after fifteen centuries, the re-appearance of the Empire on the fateful hills of Rome." And on April 15, 1939, when announcing the annexation of Albania, party Secretary Starace called the "new Albania" another indication of the "attraction which the Rome of Mussolini, perpetuating the traditions of the Rome of the Caesars, exercises over peoples."

With respect to the internal operations of the Fascist system, the Roman idea left its traces everywhere. The requirement of the "Roman salute" in place of the handshake, the regime's policy of attempting to use Catholicism as the civil religion of the state, the demographic legislation, the policy of economic "autarchy," the inculcation of an intense militarism and love of violence in the youth—all of these "aspects of the regime's practical action" become comprehensible in view of the hold which the Roman rhetoric had over the mind of the Fascist ruling elite.

The Fascist "monuments" help today's student of Fascism recreate the "Roman" atmosphere of the Italy of the 1930's. When, in 1938, the party built its *Foro Mussolini* (now called the *Foro Italico*), it outdid even the architects of the exposition grounds in slavishly counterfeiting ancient Rome. Only in size does the imitation succeed. One of the largest stadiums in Europe is the primary attraction. A second amphitheater, called the *stadio dei marmi*, is encircled by fifty giant statues representing all forms of athletic prowess (and therefore *virtus*). A large building served as the national party school

<sup>16</sup> A flood of articles on Rome and Fascism appeared at this time in Mussolini's personally edited periodical *Gerarchia*. See especially Pietro De Francisci, "Continuità di Roma," (January, 1935), pp. 6-17; Arnaldo Cervesato, "Fondazione e immagine di Roma," (April, 1935), pp. 302-306; and Nino Guglielmi, "Roma, il Fascismo, e l'Impero," (September, 1935), pp. 755-759. One of the most influential early statements of a Fascist theorist referring to the Roman tradition as the key to Fascist thought was made by Alfredo Rocco, Minister of Justice under Mussolini. This speech, given at Perugia in 1925, is translated as "The Political Doctrine of Fascism," in *International Conciliation* (October, 1926, no. 223). This essay had the express approval of *il Duce*, who wrote: "You have presented in a masterful way the doctrine of Fascism. For Fascism has a doctrine, or, if you will, a philosophy of life with regard to all the questions which beset the human mind today." (Note the *total* quality of Fascist ideology.)



for youth; on all sides of it extend black-and-white mosaics of athletes and warriors. Fascist slogans cover almost all available space between the figures. The power of repetition was evidently recognized, for over and over the black letters shout: *Duce A Noi, Duce A Noi, DuceDuceDuceDuceDuce*. A symbol of the world itself is in the center of the grounds. An obelisk towers coldly over the entrance; formerly capped with a golden tip, today the legend remains undefaced—*Mussolini Dux*. No one who enters here can but realize that the builders and makers of this monument to decadent aesthetics were genuinely self-deluded that Italy could again attain the size and power of ancient Rome. The "era of the Third Rome" was the Messianic fulfillment of history for Italian Fascism in much the same way as the establishment of the Third Reich was for the Nazis and the classless society is for the Communists.<sup>17</sup>

Heinrich Heine, in a famous passage, predicted the crumbling of "the taming talisman, the cross," and the eruption of the "savagery of the old warriors." "The old . . . gods will rise from the ancient ruins . . . rub the millennial dust from their eyes" and "shatter the . . . cathedrals." Italian Fascism attempted just such a full-scale revival of the most savage elements in the pagan tradition. It is therefore no accident that the distinguished Irish Catholic scholar D. A. Binchy greatly feared the effect Fascism would have on the Church in Italy, which Fascism sought to employ as an *instrumentum regni*.<sup>18</sup> Binchy thereby displayed a more acute understanding of the basically pagan attitudes and aims of Mussolini's regime and the extent of its destructive potentialities than does

<sup>17</sup> The question of racial theory, adopted by the Italians as official policy in the fall of 1938, has been deliberately avoided in this discussion of Fascist ideology. Although, as the memoirs of Ciano, Bottai, Leto, and others show, Mussolini, Starace, and Farinacci were personally fierce anti-semites, racism as such cannot be seen as "native" to Fascist thought. This is not to agree with those apologists who see 1938 as simply a forced but unwilling submission to Nazi policies. Rather, Mussolini and Starace seem to have regarded racism as a means of "toughening" the Italian people and imbuing them with a more consciously "imperial" spirit *vis-à-vis* the colonies. But the Italian leaders thought of racism as an expedient, not as an ideology. For discussion of the Italian anti-semitic campaign, see L. Salvatorelli and G. Mira, *Storia del fascismo* (Rome, Novissima, 1952), pp. 836, ff.; Eucardio Momigliano, *Storia tragica e grottesca del razzismo fascista* (Verona, Mondadori, 1946) and Gerald Reitlinger, *The Final Solution* (London, Vallentine, Mitchell, 1953), pp. 321-326 and 352-358.

<sup>18</sup> *Church and State in Fascist Italy* (London, 1941). For a more apologetic view of the Church under Fascism see A. C. Jemolo, *Chiesa e Stato in Italia negli ultimi cento anni* (3rd ed., Einaudi, 1955).

Arendt when she applauds the Church's early decision not to oppose Fascism as an anti-Christian movement.<sup>19</sup>

#### THE PARTY

However much Fascism may be considered an attempt to revive Roman paganism, Mussolini's regime had, thanks to modern technology, certain machinery at its disposal of which the Caesars never dreamed. These modern instruments of power made the Fascist goal of the private person's annihilation a live possibility rather than a madman's dream. The generally rather anarchistic and easy going Italians were to be transformed. "*L'uomo nuovo—il fascista*" would be like a soldier in an endless marching column: an anonymity merged in a warmongering collectivity. This transformation was to be wrought by means of the activities of a giant single party, the propaganda machinery and the secret police.

Professor H. Arthur Steiner was one of the few political scientists writing on Italian Fascism while it was yet in power who recognized that a study of Mussolini's regime had to begin with "an analysis of the functions of the . . . Party."<sup>20</sup> On the contrary, Italian political scientists usually classified the Soviet Union as exemplifying party domination over the state, Nazi Germany as exhibiting a dualism of party and state, and Fascist Italy as placing the state in predominance, with the party completely subordinated to it.

Italian scholars of jurisprudence, concerned more with delineating the *P.N.F.*'s position according to public law than with describing its actual power as a political force, continued for many years to write that in the Fascist system the party was subordinate to the state.<sup>21</sup> Fascist ideology, in contrast to Soviet

<sup>19</sup> The Church "sagely recognized that Fascism was neither anti-Christian nor totalitarian. . . ." Arendt, *op. cit.*, p. 258.

<sup>20</sup> H. Arthur Steiner, *Government in Fascist Italy* (New York and London, 1938), p. 37. However, he goes too far in describing the governmental machinery as "meaningless and formal." The power of Buffarini as Secretary of the Interior and Ciano at the Foreign Office was very real, to say nothing of Bocchini, head of the *OVRA*. But Steiner did not have available the memoirs of Ciano, Bottai, Leto, and Senise, which help to give a true picture of what the situation was among the "palace guard." As Barrington Moore has expressed it, "There appears to be a sort of symbiosis among party, police, and state administration, in which no one of them can do without the other two." This would appear to be a general rule for totalitarian dictatorships. *Terror and Progress USSR* (Cambridge, Mass., 1954).

<sup>21</sup> The literature is incredibly voluminous. The works of O. Ranalletti, G.

and Nazi thought, exalted the state, and this fact presented the defenders of the *P.N.F.*'s independence of or superiority to the state with a real problem. Party spokesmen finally resolved the theoretical dilemma in the following manner: party and state were declared to be not "opposed as if . . . in ideological contrast to one another," but rather united in the sense that "both are the state in the ethico-political sense of the term." The problem of the relations between them was one of "political practice, not theory." The party was the "dynamic, political, anti-bureaucratic" base of Fascism, while the state was the "institutional, organizing, administrative" element. The former provided the system with its "programmatic totality," the latter with its "organizational totality."<sup>22</sup> Thus, although at the outset Italian Fascist theorizing on the party differed markedly from Nazi and Soviet ideology, these contrasts became less sharp as the *P.N.F.*, in accordance with what appear to be the imperatives of totalitarian rule, expanded to wield extensive power independently of the governmental machinery.

The Fascist party, viewed historically, passed through several phases of development before maturing into a full-fledged totalitarian, hierarchical single party "superior to or commingled with" the state organization (to recall Friedrich's definition). In his recent book on political parties M. Duverger has described the *P.N.F.*'s evolution as one of continuous deterioration after the conquest of power.<sup>23</sup> Actually, a quite different pattern of development may be traced. From the conquest of power in October, 1922, until the outbreak of the Matteotti crisis in the summer of 1924, the party was extremely disorganized, with local party chieftains conducting sporadic, uncoordinated acts of violence. To meet the Matteotti situation Mussolini appointed Roberto Farinacci, the brutal and intransigent party boss of Cremona, as national Secretary. For a year and a half Farinacci did his work, and upon his resignation in 1926 the party had come to assume the rigidly hierarchical structure which characterized it from that time forward. Under Augusto Turati, who was Secretary until 1930, the party de-

Ambrosini, S. Romano, A. C. Jemolo, and G. Fragapane will give the reader a good sample of this approach.

<sup>22</sup> Cf. "Dinamica del partito," in *Notiziario del Ufficio Stampa del P.N.F.* (September 22, 1941, no. 22). See also the works of S. Panunzio and G. A. Fanelli.

<sup>23</sup> Duverger, *Les partis politiques* (Paris, 1951), p. 303.

clined in influence and power. Mussolini, busy with consolidating his power after the months of violent repression of opposition following the famous January 3, 1925, speech disbanding all parties save the Fascist, chose to use these years as a period of "normalization" of the regime. Party "extremists" were not in high favor. At that point H. W. Schneider wrote that "It now seems quite clear that the party is of dwindling importance."<sup>24</sup>

Turati was forced out as of September 24, 1930, and Giovanni Giurati appointed in his place. Giurati commenced the intensification and expansion of party activities later completed during the Secretaryship of Starace. During the decade from 1930 to 1940 the Fascist party came to approximate the position held by the single party in Germany and even in the Soviet Union. Giurati, who conducted a victorious struggle against *Azione Cattolica*, was succeeded by Achille Starace, archetype of the party militant. Under Starace the party and its numerous affiliated organizations grew to scarcely credible proportions.<sup>25</sup> Bottai in his memoirs observed wryly that, although Fascism had begun as anti-party (*anti-partito*), it had ended as hyper-party (*iper-partito*).<sup>26</sup>

The period between the end of the Ethiopian War and the beginning of World War II has been called by Luigi Salvatorelli "l'Era Starace." Except for the short-lived Social Republic, this was the most totalitarian phase of Fascism, the period of the "reform of custom" and the anti-semitic campaign. The party made itself felt everywhere. Ciano relates a conversation with Buffarini, Secretary of the Interior, on the ascendancy of the party. Buffarini sounded the "alarm bell" about what he judged to be "the dangerous hegemony of the party over all sectors of national life."<sup>27</sup> Ciano's diaries contain many in-

<sup>24</sup> H. W. Schneider, *Making the Fascist State* (New York and London, Oxford, 1928), p. 131.

<sup>25</sup> Between 1933 and 1939 the *P.N.F.* grew from 1,099,626 to 2,633,514 members. The latter figure amounted to about 6 per cent of the population, or 17 per cent of the total electorate. The youth organizations reached the 6,000,000 mark by the mid-thirties and in 1939 totalled 7,891,547. This figure actually exceeds that of the *Hitler Jugend* for the same year. The five main Fascist Associations of Civil Servants (directly dependent on the party) had 806,129 members in the fall of 1939. The party Militia claimed a membership of 763,904 in September of 1938. The *Opera Nazionale Dopolavoro*, also under party control, had 3,832,248 persons enrolled in its ranks in 1939. For complete statistics and their break-down, see the tables in the writer's Ph.D. thesis, already referred to in this article.

<sup>26</sup> Giuseppe Bottai, *Vent'anni e un giorno* (1949), p. 38.

<sup>27</sup> Galeazzo Ciano, *1937-1938 Diario* (Rocca S. Casciano, 1948), p. 276.

cidents which help to re-create the totalitarian atmosphere of "l'Era Starace."

The traits which characterized the single party in Fascist Italy fit together in a complex, helpful for comparative purposes. There are ten distinctive characteristics which the Fascist party displayed at the height of its power during the decade 1930-1940. The *Partito Nazionale Fascista*:

(1) was supported by the regime's official theory as the *permanent* single party (*partito unico*) of the dictatorship;

(2) was, in so far as internal structure is concerned, organized from top to bottom in a rigidly hierarchical manner under the immediate control of the Dictator, through the Secretary, who was the *Duce's* subordinate;

(3) maintained a "closed" rather than an "open" membership policy, allowing neither free entrance nor exit;

(4) completely controlled a whole range of associations designed to bring leisure, sport, culture and joint professional activity within the political sphere and to suppress all spontaneous social groupings;

(5) directed the regime's giant youth organization and the training schools for the "elite" of the youth;

(6) controlled the Fascist syndicates (in which membership was obligatory) and exercised the dominating influence in the regime's controlled economy (or "corporative state");

(7) exercised surveillance over the civil service, schoolteachers and university professors through its spy system, the associations, and, after 1932, enforced party membership;

(8) preserved its own armed Militia as a check on the regular army, into whose internal affairs (promotions, policies, etc.) the *P.N.F.* continually meddled;<sup>28</sup>

(9) carried on continuous propagandistic and indoctrinating

<sup>28</sup> Dr. Arendt has said that Italian Fascism "in contrast to the true totalitarian movements . . . could use such intensely nationalist instruments as the army, with which [it] . . . identified [itself]. . . ." *Origins*, p. 258. Actually, in contrast to military dictatorships in Spain and Argentina, in Italy relations with the army were almost always cool, as the rash of memoirs of ex-Generals indicates. It was with the armed Militia that Fascism identified itself. Mussolini retained the 750,000-man Militia because he did not want to be at the mercy of the army as Peron was. On party-army tensions see the transcript of the Baistrocchi trial reprinted in Emilio Canevari, *La guerra italiana* (2 vols., Rome, Tosi, 1948).

activities among its own members and among the masses, thereby making use of its "capillary" structure; and

(10) represented through its "Inner Circle" a bulwark of intransigence and extremism on questions of high policy.

It seems from the available knowledge that these characteristics of the Fascist single party were to a large degree shared by the Nazi and Soviet parties. However, again on the basis of accessible evidence, which is not plentiful, a number of these properties do not appear to have been exhibited by certain of the single parties in the "National Front" dictatorships which appeared all over Europe, especially in the decade prior to World War II. This point cannot be expanded here, but the parties of the Turkish, Portuguese, Argentine, Spanish and Vichy French regimes seem definitely to have fallen short of being either superior to or commingled with the governmental organization. The weakness of the single parties in these "minor" dictatorships may be one of the major explanations as to why they have displayed a lower level of totalitarian dynamism than have their more aggressive counterparts.

#### THE CONTROL OF MASS COMMUNICATIONS: THE PROPAGANDA MACHINERY

In common with its contemporaries, Nazi Germany and the Soviet Union, Fascist Italy developed a network of party and state agencies devoted exclusively to the control of the channels which distributed information to the public. At the beginning this machinery was only partially effective. Literature was left comparatively free, although Italian writers found it expedient to censor themselves. Non-Fascist writers, with occasional exceptions like Moravia and Levi, evaded political topics and retreated into the literary essay. Except for Croce, no non-Fascist scholar could write on recent or contemporary history, and even Croce did not carry his *History of Italy from 1871* beyond 1915. Movies were subject to fairly strict control by the Institute *LUCE*. The state-owned radio was of course thoroughly Fascistized; a phenomenal amount of time was taken up by political broadcasts. The theater was somewhat less controlled at first than the cinema, but after 1935 the



stage degenerated sharply, producing banal and politicized plays.

The Italian press, which Mussolini liked to call "an orchestra played in concert, although on different kinds of instruments," was closely supervised from the outset. Anti-Fascist editors of *La Stampa* and *Corriere della Sera* were forcibly removed; indeed, with Albertini's ouster from the direction of the latter journal early in the history of the regime, liberty of the press was dead. The press was censored and controlled by the Press and Information Office of the *Capo del Governo*. This office was closely supervised by Mussolini and the party leadership.

Monotonous and conformist as were the Italian press, radio, cinema and theater from the very beginning of the dictatorship, not until the middle and late 'thirties did Fascism proceed to use systematically these mass media for what one scholar has termed the *Gleichschaltung* of the nation.<sup>29</sup> On June 1, 1937, all of the various Fascist censorship offices were abolished, and the control of the press (except for party journals), radio, cinema, live productions, periodicals and books passed to the new Ministry of Popular Culture (known in common parlance as "Minculpop"). No longer was the regime concerned principally with negative censorship. Through the new Ministry a positive campaign of indoctrination was carried on.

Immediately after the fall of Fascism, an Italian scholar managed to acquire a considerable number of Minculpop's orders to the press, and he published an instructive sampling of them.<sup>30</sup> These *note di servizio* gave detailed commands on the content of certain articles, the space and emphasis to be accorded them, and even the size type to be used in headlines. The directives on the anti-semitic campaign and the "reform of custom" are especially interesting, as are those ordering the press to follow the latest twist in Fascist foreign policy.

Supplementing the work of the Ministry of Popular Culture was the propagandizing activity of the party.<sup>31</sup> In the national

<sup>29</sup> See Salvatorelli and Mira, *op. cit.*, pp. 752-754 for a discussion of the Ministry of Popular Culture.

<sup>30</sup> Francesco Flora, ed., *Stampa dell'Era Fascista. Le note di servizio* (Rome, Mondadori, 1945).

<sup>31</sup> Two factors should be kept firmly in mind while considering the propaganda activities of the *P.N.F.* The first is that the party was the single party of the regime and that as such it had a monopoly in this field. Without this monopoly many of its propaganda activities do not appear to be very different from those



headquarters of the *P.N.F.* there was an *Ufficio Propaganda del Partito*, which, through its subdivisions in each provincial and local party organization, coordinated and administered the party's activities in this area. In all the subdivisions of the party organization itself, the youth organizations, the *Dopolavoro*, the associations and the syndicates, a continuous indoctrination process went on.

Some of the campaigns were directed at immediate problems. For instance, with the introduction of the anti-semitic legislation of 1938, the party initiated thousands of special meetings at all levels of its organization designed to arouse hatred of the Jews. And the so-called Institute of Fascist Culture, under direct party control, conducted a nation-wide series of lectures for the Italian populace on such topics as "Purity of the Race from Roman Times," "Liberation from Zionism," "The Jew and Modern Culture" and "Race and the Problems of Colonization."

Only part of the *P.N.F.*'s propaganda program was intended to elicit enthusiasm for the regime's ephemeral policies, whatever they might be at a given time. In addition to this objective, the party took upon itself the permanent task of inculcating acceptance of the general ideology and organizational techniques in the masses. The great plebiscites offered a particularly good opportunity for this second type of propaganda. These orgies occurred only once every five years, however. Year in and year out other party propaganda activities proceeded. Every year a series of "Conversations on Fascist Culture" was given in every province to the older members of the youth organizations. Four lectures were on the history of the Fascist Revolution, five on the political and economic institutions and doctrines of Fascism, and three on war, imperialism and foreign policy.<sup>32</sup> For the working class the party sponsored through the *Dopolavoro* a yearly course given in the local syndical halls on the history of the Revolution,

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of a constitutional party in a parliamentary system. A second point to be borne in mind is that the party propaganda was "reinforced" by the regime's system of terror.

<sup>32</sup> The 1939 courses were held in a total of 7,241 local GIL commands, taught by 18,880 instructors, and attended by 6,864,390 youths. In *Atti del P.N.F., Foglio di disposizioni* no. 1313, April 20, 1939.

the organization of the *P.N.F.* and the "corporative state." Similar programs were given for the rural populace.

Party and Ministry of Popular Culture were under the Italian Fascist dictatorship united in a drive to elicit mass ideological conformity. Their efforts reveal the mania for mass support which so characterizes the three major dictatorships of recent times. Activities in the propaganda field also demonstrate the crucial importance to these modern dictatorships of up-to-date techniques of mass communication as instruments for the manipulation of public opinion. As one writer neatly expressed it: "The Genevan exiles in Elizabeth's first Parliament might [have been] totalitarian by temperament, but they lacked a radio station."<sup>33</sup>

#### THE TERROR

Of all the aspects of Italian Fascism, we know the least today about the terror. However, since the war two memoirs have been written which illuminate this subject somewhat.<sup>34</sup> Prior to 1926 the Italian police system was in a state of terrible disorganization and inefficiency. In September of that year Arturo Bocchini, a "career" man and formerly Prefect of Bologna and Brescia, replaced Crispo-Moncada, who had been inept in dealing with the most recent attempt on Mussolini's life. Bocchini set about immediately to modernize police equipment, to improve the training schools and to expand the service. In 1927 he established an *Ispettorato Speciale di Polizia* which mushroomed into the regime's political police. The new organization came to be known as *OVRA*, or *Organizzazione di Vigilanza per la Repressione Antifascista*.

At first Bocchini was little more than a docile instrument of the party and then of the Ministry of the Interior. As the years progressed, the *Capo della Polizia* attained a position of independent power. He was, however, never as powerful as was Himmler in the Nazi state, if for no other reason than that the scope of the terror in Italy was less.

Most foreign students of Fascism writing during the heyday

<sup>33</sup> Bernard Crick, in *Confluence* (December, 1954), p. 453.

<sup>34</sup> Guido Leto, *OVRA. Fascismo-Anti-Fascismo* (Bologna, Cappelli, 1952) and Carmine Senise, *Quando ero Capo della Polizia* (Rome, Ruffolo, 1946). Leto, as deputy to Bocchini was head of the *OVRA*, until the latter's death in 1940.

of the regime made far too little of the importance of the terror as a permanent part in the machinery of the dictatorship. On the other hand, there were also published some undoubted exaggerations on this subject.<sup>35</sup> In his recent volume on the Special Tribunal for the Defense of the State, Fascist Italy's Star Chamber, Cesare Rossi has placed the total number of persons "tried" during that body's twenty-year existence at 21,000.<sup>36</sup> This figure does not take account of the numbers of persons taken into "protective custody" and assigned to "confinement" (*confino*) on one of the penal islands or in isolated areas of southern Italy. These individuals were detained, often permanently, without even the excuse of a trial. Many times they included persons previously tried and found not guilty by the courts. Nor do the statistics account for the numerous raids by party *squadristi* directed against those Italians whom the party deemed "suspect." However, the detention camps on the islands and mainland appear never to have held more than 5000 inmates at any one time, excluding the period of the Social Republic (1943-1945), when the terror had a far greater scope. These are small figures compared to Nazi and Soviet operations in this area.

Leto has written of the conditions existing on the penal islands: "Many have asked, . . . especially after the terrifying reports which have come out of Germany . . ." how Italian detention camps compared with those of the Nazis. "On this point . . . although excesses undoubtedly occurred, it is opportune to say a word of truth and clarification for our good name and our humanitarian tradition. . . ."<sup>37</sup> Leto has presented an unquestionably idyllic account of life on the islands;<sup>38</sup> the fact remains that not even the most violently anti-Fascist Italians have contended that conditions there,

<sup>35</sup> H. Hessel Tiltman wrote that "Not even in Soviet Russia has personal liberty suffered a more complete eclipse than it has in Italy. . . ." *The Terror in Europe* (London, 1931), p. 330.

<sup>36</sup> C. Rossi, *Il tribunale speciale* (Milan, Ceschina, 1952), p. 7.

<sup>37</sup> Leto, *OVRA*, pp. 61-64.

<sup>38</sup> At least two accounts of the conditions on the penal islands written by non-Fascists have appeared and they paint a much harsher picture than does Leto. Stefano Jacini, a respected leader of today's Christian Democratic party, has spoken of the use of torture to extract information, isolation with bread and water for up to three months, wretched sanitary conditions, violence and sadism among certain guards, and so on. *Il regime fascista* (Milan, Garzanti, 1947), pp. 170, ff. Massimo Salvadori, in *Resistenza ed azione* (Bari, Laterza, 1951) tells of his own experience in *confino* on the island of Ponza.

even at their worst, began to approximate either in scope or intensity the scientific cruelty of the Nazis.

But these observations should not obscure the fact that the Fascist terror was very real and that Italian Fascism was not "just another despotism" which was "really not so bad after all." The scope of the terror is not the only factor to be considered. Fascist Italy was a fear-ridden society in which a man could be taken from his domicile and at the very least be threatened or beaten because of some vague suspicion lodged with the police or the party. There was no way for the average citizen to know the numbers of people in *confino* or how they were treated; the mere existence of the institution was enough to cause universal anxiety. Ignazio Silone captured this atmosphere of terror under Italian Fascism in his *Bread and Wine*:

Minorca: It is well known that the police have their informers in every section of every big factory, in every bank, in every big office. In every block of flats the porter is, by law, a stool pigeon for the police. In every profession, in every club, in every syndicate, the police have their ramifications. Their informers are legion, whether they work for a miserable pittance or whether their only incentive is the hope of the advancement in their careers. This state of affairs spreads suspicion and distrust throughout all classes of the population. On this degradation of man into a frightened animal, who quivers with fear and hates his neighbor in his fear, and watches him, betrays him, sells him, and then lives in fear of discovery, the dictatorship is based. The real organization on which the system in this country is based is the secret manipulation of fear.<sup>39</sup>

It is precisely this atmosphere which Sig. Leto omits describing, although it is an indispensable background for the reading of his book.

#### THE BALANCE SHEET

It is clearly on the last of Friedrich's four criteria, the terror, that Fascist Italy fell short of the totalitarian mark. As Arendt has emphasized, the totalitarian terror is not concerned solely with the "suspect" but also with the "potential enemy."<sup>40</sup> The

<sup>39</sup> I. Silone, *Bread and Wine* (New York, 1937), pp. 260-261.

<sup>40</sup> Arendt, *op. cit.*, p. 401.

mass imprisonment and destruction of entire occupational or ethnic groups, chosen on the basis of ideological reasons, simply did not occur under Fascism until the Salò Republic, and even here the problem of the extent of German influence presents itself. This does not mean that the possibilities were not there. In spite of the fact that his internal position was never more secure, Mussolini insisted that the terror be heightened in the late 'thirties.<sup>41</sup> The party's campaign against the "bourgeoisie" and the Jews after 1937 offered opportunities for the more "developed" form of terror. But the advent of the war suspended these projects for the time being.

Italian Fascism encountered two barriers which slowed down its rate of totalitarian development. The first of these impediments was the Italian people. While it cannot be truthfully said that any people is suited for totalitarianism, it is notorious that the Italians were *not* so constituted. Mussolini regarded contemptuously the Italians as inferior "material" for his dictatorial work of art, and, in his personal comportment, always strained to act the reverse of the stereotype Italian. Indeed, it was for the purpose of transforming the Italian who liked to sing in the streets, talk and gesture a great deal, and take a long *siesta* that the party undertook its "reform of custom." The second hindrance was the relative smallness of Italy's population and territory. Arendt has correctly observed that smaller countries "simply [do] not control enough human material" to allow for the required "great losses in population." Even Nazi Germany did not reach its zenith in this sphere of the terror until the conquests of the War gave it control over a sufficient number of people.

If for these reasons Fascist Italy fell short in the matter of the terror, there is little doubt that it was fully totalitarian with reference to the other three criteria. A "nationalist dictatorship" like Franco Spain, on the other hand, could never claim this record; ideology is nebulous or non-existent, the party is miserably weak and the Spanish educational system and propaganda machinery are in the hands of the Roman Catholic Church.

It is true that Italian Fascist ideology lacked systematic

<sup>41</sup> Ciano, *Diario, 1937-1938*, p. 207. Mussolini intended a "third wave" of terror and the introduction of concentration camps on the German model.

formulation in comparison with Marxism-Leninism. Yet Fascism did have an ideology in the call of Rome. In this concept was implied the chiliasm and "political messianism" (Talmon) so characteristic of the totalitarian ideologies of our time. The frequent clashes Fascism experienced with the ecclesiastical authorities, especially in the area of youth education, resulted from the regime's attempt to enforce an opposing ethical system on the Italian people.

Italian Fascism was no comic opera, nor was it a South American palace revolution. It was a political religion, equipped with the machinery necessary to realize its program. During its twenty-odd years of existence the Italian Fascist dictatorship developed relentlessly towards the totalitarian pattern. The twilight shadows of late Italian Fascism were inexorably deepening into totalitarian night.

## THE POLICY OF TAKE-OVER: THE STAGES OF TOTALITARIAN DEVELOPMENT IN EASTERN EUROPE

*Richard J. Medalie\**

### SOME THEORIES OF TOTALITARIAN DEVELOPMENT

ON May 9, 1941, Tito, the future leader of Yugoslavia, received a secret communiqué from the Comintern. Among its instructions was the following:

The time has now come when we must take new decisive steps toward world revolution. The obstacles to be surmounted are formidable and call for a new tactical flexibility. . . . The Communist world revolution must be presented as a series of measures to achieve "real democracy," . . . Immediately after the seizure of power, the Central Committee will set up a new government. This shall be representative of the broad masses of the people and appear democratic. . . .<sup>1</sup>

Here was a blueprint for the future sovietization of Yugoslavia, a pattern of revolution. Here was an ominous prophesy of the events which were soon to sweep through Eastern Europe. The time came; the prophesy matured. From the end of World War II on, Albania, Yugoslavia, Bulgaria, Rumania, Hungary, Czechoslovakia, Poland—each of the Eastern European countries in its turn fell victim to the Soviet Union and communism.

What was the pattern of the communist conquest? Several attempts have been made by students of Eastern Europe to erect a conceptualized model of the pattern of events in the satellite countries and from this model to construct a theory of the stages of totalitarian development. Each of these scholars, unfortunately, has constructed a model of the Eastern European revolution which only partially takes into consideration the full sequence of events, the particular timing of the events and their relationship to the broader struggle for power be-

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<sup>1</sup> Raditsa, Bogdan, "The Sovietization of the Satellites," *Annals of the American Academy of Political and Social Science: Moscow's European Satellites*, 271, September, 1950, pp. 124-25.



tween East and West. No one, up to this time, has attempted to relate all of the varied factors within a single conceptual framework.

For example, Hugh Seton-Watson, a Western observer, is primarily concerned with the pattern of the communist seizure of power. In his theory he outlines three stages of development. In the first stage there exists a "genuine coalition" of various political parties, each having its own party organization and each differing in ideology, program and social basis. During this stage, the Communists take over the instruments of state power. In the second stage, only a "bogus coalition" exists. All the peasant and bourgeois parties have already been thrown into opposition, but are still tolerated. The government still contains non-communist parties, but the leaders of these parties are chosen already by Communists. "Monolithic unity" is the basis of the third stage. The Communists establish a centrally disciplined National Front, which they completely control. The Social Democrats and Communists fuse into a United Workers' Party.<sup>2</sup> In applying his theory, Seton-Watson explains that not all of the countries went through all of the stages. Rumania, Bulgaria, Hungary and Czechoslovakia began their post-war existence in the first stage, Poland in the second and Albania and Yugoslavia in the third. Furthermore, while most of the countries went from one stage to the other in logical progression, Czechoslovakia skipped directly from the first to the third. Finally, each of the countries moved from one stage to the other at different times. Thus while Seton-Watson reveals shrewd powers of observation in constructing his theory, he is not successful in the following tasks: fitting all the countries within each of the categories, structuring a significantly meaningful time-table of development and relating the development to the international scene.

Another writer, Miss Doreen Warriner, a Western pro-communist sympathizer, delineates the stages in the following manner: (1) 1944-45: the uniting of all non-fascist parties into national fronts under communist leadership in order to rid the country of fascists and collaborators; (2) 1945 to 1947-48: the defeating of the bourgeois opposition represented by right-

<sup>2</sup> Seton-Watson, Hugh. *The East European Revolution*, 2nd edition, London, 1952, pp. 169-71.

wing parties; (3) 1947-48 to present time: the merging of the parties and the defeating of the church and *kulaks*.<sup>3</sup> Miss Warriner, at least, attempts to structure her stages in chronological order, and therefore provides a more uniform pattern of development for the countries. Unfortunately, her powers of observation are not as profound as Seton-Watson's. As a result she insists that the purging of fascist-collaborators is a separate stage. She also insists on labeling all of the forces which the Communists attacked as right-wing, reactionary, fascist, bourgeois and the like. Finally, she does not specifically relate each stage of development to international events.

A third writer, the Soviet theoretician, N. P. Farberov, is also concerned with the stages of development in Eastern Europe. While his analysis is obscured by communist terminology, it nevertheless testifies to a well-thought-out theoretical construction. Farberov sees the development in two stages. The first stage lasts from 1944-45 until the middle of 1947-middle of 1948. During this period, the countries concerned rid themselves of the last vestiges of fascism, undertake the reconstruction of the economy, and "democratize" the socio-political life (i.e., the Communists gradually take over the instruments of power). The second stage extends from the middle of 1947-middle of 1948 until the present day. During this period, the reactionary elements are deposed, the parties representing the proletariat are united, the National Fronts are restructured to guarantee communist supremacy, the government is reformed to consolidate the communist power, the various deviations within the ranks of the communist parties are dealt with and collectivization and strengthening of the socialist sector of the economy are undertaken.<sup>4</sup> By and large, this formulation, with modifications, at least attempts to account for the events as well as their timing. The main difficulty is that the categories constructed are so broad and all-inclusive that certain distinctive patterns are obscured.

What are the discernible stages of totalitarian development in the satellite countries? What is the most useful type of conceptual framework within which one could unify all of the

<sup>3</sup> Warriner, Doreen. *Revolution in Eastern Europe*, London, 1950, p. 16.

<sup>4</sup> Farberov, N. P. *Gosudarstvennoe Pravo Stran Narodnoi Demokratsii*, Moscow 1949, pp. 17-23.

diverse factors into a single theory? This paper will formulate a revised model of the stages of development in the Eastern European countries. In general outline, the stages may be delineated as follows:

First stage: Moderation. 1944-45 to middle of 1947.

Destruction of the old ruling class.

Disruption of the coalition.

Second stage: Tightening-up. Middle of 1947 to end of 1948.

Destruction of the opposition.

The purge of the coalition.

Third Stage: Uniformity. Middle of 1948 to 1953.

The purge of the Communists.

The Sovietization of society.

In addition to a more detailed discussion of the events as outlined above, this paper will constantly attempt to relate the events to the international situation and to the communist theory of People's Democracy, as the Eastern European satellites came to be known.

#### THE POLITICAL BACKGROUND

*Postwar Political Conditions.* Before analyzing the events that finally led to the consolidation of power in the satellite countries, let us examine the peculiar post-war political conditions that either hindered or facilitated the drive toward Communist power.

Bulgaria, Rumania and Hungary presented the greatest difficulty to the Communists in their drive for power. In Rumania and Hungary, their non-Slav origin, the strong Catholic elements in the latter, and the traditional hostility toward Russia greatly hindered Communist development. The power drive was facilitated to a greater extent in Bulgaria because of its common Slav background and historical friendship with Russia. The main advantage to the Communists was the stationing of Soviet troops in these countries as occupation authorities. All Allied Control Commissions were actually under Soviet power. Thus, whenever the opposition became too difficult for the Communists, the Soviet authorities could step in to assure communist success.

Czechoslovakia was a different story. It was the only country in which the war-time government-in-exile under Benes was allowed by the Soviet Union to return and participate as a true equal in the postwar government. Much of this Soviet tolerance had to do with the peculiar nature of Czechoslovakia. Not only did the country have a Slavic background, but the spirit of pan-Slavism was a real force. Extremely friendly relations existed between Czechoslovakia and the Soviet Union. Benes who returned as President of the Czechoslovak Republic, though a National Socialist, was definitely pro-Russian. There was an implicit belief that "the Soviet Union was . . . interested only in 'friendly' neighbors and would permit government processes . . . to develop along the path of authentic parliamentary democracy."<sup>8</sup> Furthermore, the disillusionment with France and Great Britain because of Munich led many of the Czechoslovaks to believe that they could expect little from the West and therefore could look to no other alternative but Moscow. A further point in favor of the Communists was the actual popular support which they possessed. These factors assured the Soviet Union and the local Communists the possibilities for final control whenever they wanted it. With the final assurance of communist participation in the post-war government, the question of the seizure of power became a matter of patience and time.

In Poland the Communists found themselves in a slightly different situation. Though Poland was a Slav nation, the centuries of wars and conflicts with the Russians had left bitter memories. The insistence by the Western Powers that Mikolajczyk's Polish Peasant Party be included in the new government as a representative of the war-time government-in-exile provided the discontented populace with a standard bearer around whom they could rally. For several years, Mikolajczyk offered effective opposition to the Communists. On the other hand, the major factor assisting the Communists in their bid for power was the so-called liberation of Poland by the Red Army. It brought in its "baggage car" a new communist-controlled government, replete with three Polish divisions in the Red Army and a Soviet-style secret police. To all intents and

<sup>8</sup> Sharp, S. L. *New Constitutions in the Soviet Sphere*. Washington (Foundation for Foreign Affairs), 1950, p. 8.

purposes, the Lublin Provisional Government, as it was called, was in complete control of the government apparatus even prior to the end of the war.

Yugoslavia and Albania presented no problems to the Communists. The decisive struggle for power had been won even prior to the end of the war. During the war, the resistance movements had come under the complete control of the Communists. During 1943-44, the resistance movements in both countries had created provisional governments with Tito as President in Yugoslavia and Enver Hoxha as President in Albania. The kings of both countries had been forbidden to return until the question had been decided by popular referendum. The opposition, the Chetniks in Yugoslavia and the Balli Kombetar in Albania, had been defeated in civil war which had raged throughout the countries concurrently with the fight against the fascist invaders. When the enemy was forced out of the country, the communist-dominated, resistance-movement provisional governments took over. While Yugoslavia was forced for a few short months to accept in the government representatives of the war-time government-in-exile, Albania did not even have to bother with such formal preliminaries. By the end of the war, Yugoslavia and Albania were safely within the Soviet camp.

In summary, despite the obstacles to the final communist control of power, certain factors; namely, (1) the occupation of Bulgaria, Rumania, and Hungary by the Soviet forces, (2) the trust and friendship of the non-communist parties for the Soviet Union and the popular support of the Communists in Czechoslovakia, (3) the importing of a communist-controlled regime by the Red Army in Poland, and (4) the rise to power of the Communists prior to the end of the war in Albania and Yugoslavia, almost guaranteed final success to the communist venture.

*Postwar Political Parties.* In all the countries, with the possible exception of Czechoslovakia, no previous government which had either existed during the war or had gone into exile was allowed to be reestablished. No party which had been compromised during the war by collaborating with the invaders was allowed to participate in political life. Furthermore, as a general rule, no formal opposition party was allowed to be

formed during the beginning months of the postwar period. All parties which participated in political life were required to be members of the government coalition.

In Bulgaria, Rumania, Hungary and Czechoslovakia the government blocs were composed of genuine coalitions of several autonomous political parties. In Poland the government bloc was a bogus coalition and with the exception of Mikolajczyk's party, all the non-communist parties were under communist control. Finally, in Albania and Yugoslavia, the governments were completely communist dominated, with only the Communist Party having an independent existence.

A particular characteristic of all of the countries of Eastern Europe, except for Czechoslovakia, was that they were predominantly agrarian states. This being so, the peasant or agrarian parties in these states enjoyed a very strong measure of support from the populace. In Hungary, the power of the peasant party had been so great that it received an absolute majority in the first post-war election, which caused no end of problems to the Communists. As a result, the predominant party which potentially was the greatest threat to the communist bid to power was the peasant party in each of the states.

The following parties existed in all of the coalitions:

*Communist Dominated Parties:* In all countries a Communist Party existed. In some of the countries, such as Bulgaria and Poland, the Communist Party went under the name of "Workers' Party" in order to delude the others. Two Communist Parties existed in Czechoslovakia: one for the Czechs and the other for the Slovaks.

Social Democratic Parties existed in all countries. In the Central European countries of Poland, Czechoslovakia and Hungary, where they had a long tradition, the Social Democratic Parties were stronger than in the Southeastern area of Rumania and Bulgaria. As with the Communist Party, there existed two Social Democratic Parties in Czechoslovakia.

Most Peasant Parties were not communist dominated at the beginning, but only became so later. Only in two countries did these so-called "rural branches of the Communist Party" exist from the very beginning: the Ploughman's Front in Rumania and the government-sponsored Peasant Party in



Poland. Later on, the National Peasant Party of Hungary became a Communist front.

Bourgeois or Liberal Parties included the Tartarescu Liberals in Rumania, the Zveno and Radical parties in Bulgaria, and the Democratic Party and later the Labor Party in Poland.

*Potential Opposition Parties:* Peasant Parties included National Peasant Party under Maniu in Rumania, the Left-wing Agrarians under Dimitrov and Petkov in Bulgaria, the Small Holder party under Kovacs and Nagy in Hungary, and the Polish Peasant Party of Mikolajczyk in Poland.

The Liberals of Bratianu in Rumania; and the Czech National Socialists under Benes, the Czech Populist Party, the Slovak Freedom Party and the Slovak Democrats in Czechoslovakia were the representatives in the Bourgeois or Liberal Party category.

Social Democratic Party factions were the Petrescu wing of the Social Democrats in Rumania and the Chesmedijev-Lulchev wing of the Social Democrats in Bulgaria.

Finally, in Yugoslavia there was the special case where the representatives of the exile-government, Subasic, Grol and Sutej participated in the post-war government coalition for several months because of Western insistence.

#### THE FIRST STAGE: MODERATION

The first stage lasted from 1944-45 until the middle of 1947. Except in Yugoslavia and Albania, the policy in each one of the countries was one of moderation. There were obvious reasons for it. The plan to transform these countries into satellites of the Soviet Union was a difficult one to accomplish. Any attempt to hasten it might well have led to trouble. The mere technical tasks of ruling the countries presented peculiar problems. Administrative and economic tasks required the work of experts. In many of these countries, the Communists, being a small and relatively young party, thought it wise to use the other parties to their advantage. Time was necessary to assuage the peasants' fears about collectivization; time was necessary to convince the other parties that the Communists were after the same goals as they; time was necessary to grasp more firmly the instruments of power.<sup>6</sup> Furthermore,

<sup>6</sup> Revai, Josef. "On the Character of Our People's Democracy." *Társadalmi*



the Eastern European area was perhaps the most devastated during the war. Time and patience were again needed to begin the tasks of reconstruction and rehabilitation of the countries. Any violent upheavals or social transformations may well have delayed the economic reconstruction.<sup>7</sup>

On the international scene, it seemed possible that the Soviet Union feared to jeopardize the unique opportunities for the Communists to come to power in France and Italy.<sup>8</sup> Moreover, the Soviet Union was undoubtedly concerned about a premature disruption of the wartime alliance.<sup>9</sup> The Potsdam agreement had specifically called for free elections in Poland. Recognition of the Bulgarian, Rumanian and Hungarian governments depended on Western consent. It was therefore practical as well as necessary to gain power by parliamentary methods in order to avoid giving the Western powers a pretext for interference. The strategy worked and the West retaliated only by repeated protests against the throwing of parties into opposition, the conduct of elections or the arrest of some opposition leader.

*People's Democracy: A New Form of Democracy.* The strategy at the beginning was to hide behind the mask of democracy. Communists tried to encourage the belief that there existed an "adapted" form of communism, which could allow cooperation in genuine coalition with democratic non-communist elements. Slogans hailing the class struggles were discretely replaced by obscure slogans about democracy.<sup>10</sup> The emphasis on moderation was a tactic used by the Communists in order to assuage the fears of the contending forces. As Josef Revai of Hungary admitted later in 1949:

. . . we said that the People's Democracy was a . . . popular kind of bourgeois-democracy. . . . It was correct at that time to stress that the issue was not a choice between Socialist or bourgeois private property, but rather the following: Should we compromise with the forces of the old system or should we liquidate them. It

<sup>7</sup> Szemle, March-April, 1949, p. 45 and p. 57; translated in *Foreign Affairs*, 28:1, October, 1949, pp. 143-52.

<sup>8</sup> *Ibid.*, p. 45.

<sup>9</sup> Taborsky, Eduard. "Government in the People's Democracies," *Annals of the American Academy of Political and Social Science: Moscow's European Satellites*, 271, September, 1950, p. 56.

<sup>10</sup> Borkenau, Franz. *European Communism*. London, 1953, p. 504.

<sup>11</sup> Sharp, *op. cit.*, p. 9.

was correct that in the fight against big capital, we did not stress that this was a transition into the struggle for socialism, but that the measures initiated against big capital meant at the same time the protection of small private properties. *It was correct not to show our cards*<sup>11</sup> (*italics—RM*).

There appeared to be an attempt by the Soviet Union to play its role discretely behind the scenes. It is true that tribute was paid to the Soviet Army for liberating Eastern Europe. Many of the communist leaders emphasized that the mere existence of the Soviet Union made the revolutionary changes in the countries possible.<sup>12</sup> Some Soviet spokesmen stated that without the support of the Soviet Union, the People's Democracies would have had the fate of Greece.<sup>13</sup> Others even went so far as to affirm that without the Soviet Union, "the whole world would be under the yoke of reaction and barbarism."<sup>14</sup> At the same time, however, the theoreticians scrupulously avoided saying that Yugoslavia and Albania had been liberated by Soviet forces. In fact, eulogies were delivered about the brave and successful Yugoslav Partisan movement.<sup>15</sup>

In addition, satellite and Soviet spokesmen alike continually denied that the Soviet Union had predominantly brought about the revolutions in Eastern Europe<sup>16</sup> or that the Soviet experience could be applied to the new circumstances.<sup>17</sup> In keeping with the communist attempt to conciliate national and non-communist feeling, the communist leaders bent over backwards to emphasize the differences between the Soviet and Eastern European developments. As Josef Revai said, ". . . we emphasized the differences between the development of the Soviet Union and our development into a People's Democracy instead of stressing the similarity, the substantial identity of the two developments."<sup>18</sup>

<sup>11</sup> Revai, *op. cit.*, p. 147-48.

<sup>12</sup> Sharp, *op. cit.*, p. 12.

<sup>13</sup> Varga, E. S. "Demokratiya Novovo Tipa," *Mirovoe Khozyaistvo i Mirovaya Politika*, 3, March, 1947, p. 4.

<sup>14</sup> Trainin, I. P. "Demokratiya Osobovo Tipa," *Sovetskoe Gosudarstvo i Pravo*, 1947, I: p. 8.

<sup>15</sup> Varga, *op. cit.*, p. 4; Leontiev, A. "Ekonomicheskie Osnovy Novoy Demokrati," *Planovoe Khozyaistvo*, 4, 1947, p. 66.

<sup>16</sup> Sharp, *op. cit.*, p. 12.

<sup>17</sup> Skilling, H. Gordon. "People's Democracy in Soviet Theory," *Soviet Studies*, III, 1, 2, July, October, 1951, p. 139.

<sup>18</sup> Revai, *op. cit.*, p. 148.

In September, 1946, Dmitrov, the communist leader of Bulgaria, proclaimed that "Bulgaria will not be a Soviet Republic, it will be a People's Republic. . . . There will be no dictatorship in the republic. . . ." <sup>19</sup> Horvath Martin of Hungary went so far as to consider People's Democracy not only as "the most progressive form of bourgeois democracy," but "its only progressive form." <sup>20</sup> Even the Soviet economist, E. S. Varga, at first placed the People's Democracies in the bourgeois-democratic camp by noting the predominance of "state capitalism" in these countries. <sup>21</sup>

As time progressed, the theorists refined the definition of the essence of the new states. There was recanting by some who had previously likened the states to bourgeois democracy. <sup>22</sup> Now the emphasis was rather that the People's Democracies represented some sort of a synthesis between capitalism and socialism. Some considered the states to be a bridge, a compromise between the Socialist East and the Capitalist West. <sup>23</sup> "The New People's Democracies are like a bridge thrown between two epochs," as the Italian Communist, Eugenio Reale, expressed it. <sup>24</sup> By far the most authoritative though conflicting definitions of People's Democracy came from the Soviet theoreticians, A. Leontiev, E. S. Varga and I. P. Trainin.

Leontiev was so impressed by the uniqueness of the new states in Eastern Europe that he affirmed:

. . . neither Marx nor Lenin foresaw or could foresee such a form [of state] . . . as the New Democracy, because it was engendered by completely specific historical situation, by special conditions which were impossible to foresee beforehand. <sup>25</sup>

Varga considered it wrong to have believed that the political supremacy of the workers could be realized only in the form of a

<sup>19</sup> Chervenkov, V. "The Activities of the Bulgarian Workers' Party," *For a Lasting Peace, For a People's Democracy*, 3, December 15, 1947, p. 2 (organ of the Cominform, Belgrade, November 1947-June 15, 1948; Bucharest, July 1, 1948—).

<sup>20</sup> Kardelj, Edward. *On People's Democracy in Yugoslavia*. New York (Yugoslav Information Center), 1949, p. 8.

<sup>21</sup> Varga, E. S. "K Voprosu o Demokratii Novovo Tipa," *Mirovye Khozyaistvo i Mirovaya Politika*, 5, May, 1947, p. 126.

<sup>22</sup> *Ibid.*

<sup>23</sup> Bierut, B. "Ideological Basis of the United Workers' Party of Poland," *For a Lasting Peace, For a People's Democracy*, 1(28), January 1, 1949, p. 2.

<sup>24</sup> Kardelj, *op. cit.*, p. 5.

<sup>25</sup> Leontiev, *op. cit.*, p. 69.

Soviet system. On the contrary, the new states in Eastern Europe clearly showed that this worker supremacy was possible by means of "the preservation of the external form of parliamentary democracy."<sup>26</sup>

The social order of these states differ from all states known by us so far. It is something completely new in the history of mankind. It is not a dictatorship of the bourgeoisie, but neither is it a dictatorship of the proletariat. . . . They are not capitalist states in the usual sense of the word. However, neither are they socialist states.<sup>27</sup>

Trainin, on the other hand, took exception to calling these states new democracies in contrast to the old bourgeois democracies. The New Democracy, he stated, was the Socialist Democracy of the Soviet Union. He also took exception to calling these states People's or Popular Democracies. On the contrary, it was the Socialist Democracy which was a Popular Democracy because it served the interest of the people. He therefore considered that it was more correct to say that these states were democracies of a "special type." They developed, he said, under historical conditions during the course of the war and after it; they were a product of the conditions created by the battle between the two basic or classic types of democracy—proletarian (socialist) and bourgeois.<sup>28</sup> He added that while it was true that land reform had been introduced and some industries had been nationalized, it would be wrong to consider the economy a socialist one, since private property was still preserved. They were thus to be considered neither bourgeois nor socialist democracies,<sup>29</sup> having both capitalist and socialist productive relationships within them.<sup>30</sup>

Varga amplified the characteristics of the economies of these countries by saying that all feudal remnants, all landlords had been liquidated. On the other hand a system of private ownership of the means of production still existed, but "the large-scale enterprises in the sphere of industry, transport and credit are state-owned. . . ."<sup>31</sup>

<sup>26</sup> Varga, *op. cit.*, p. 13. (see note 13 above).

<sup>27</sup> *Ibid.*, p. 3.

<sup>28</sup> Trainin, *op. cit.* I, p. 3.

<sup>29</sup> *Ibid.*, I, p. 1.

<sup>30</sup> *Ibid.*, I, p. 4.

<sup>31</sup> Varga, *op. cit.*, p. 3. (See note 13 above).

Dmitrov of Bulgaria added:

Bulgaria will be a People's Republic in which private property, acquired by labor will be protected by the state authorities . . . , but in which big capitalist profiteering private property will not be allowed to doom the laboring people.<sup>32</sup>

The Polish Communist, Boleslaw Bierut, defined the essence of the new social and economic order as one in which there was specific harmony of the two factors; on the one side, the leading role of the state . . . on the other side, the spirit of enterprise, the energy and free initiative of the mass of independent entrepreneurs. . . .<sup>33</sup>

Gradually, as a corollary to the theory that the People's Democracy was a new or special type of state, being neither a dictatorship of the bourgeoisie nor a dictatorship of the proletariat, there evolved the idea that each of the nations were developing along an independent path, determined by the specific conditions of the historical development of each country.<sup>34</sup> There was talk of a special Bulgarian, Polish or Czechoslovak road of development. From this idea, it was only a step to the thesis that the nations could very well make the transition from capitalism to socialism under the conditions of preserving the present state form of power.<sup>35</sup> The type of economic planning present in the People's Democracies was quite sufficient to guarantee the development of these countries in the direction of socialism.<sup>36</sup> There was the feeling that the class struggle could be gradually toned down. The path to socialism could be achieved by the "harmonious combination of the state sectors in the national economy—the state, cooperative and private sectors,"<sup>37</sup> by the reconciliation of the socialist and capitalist elements. In fact, it was thought that the People's Democracies, in contra-distinction to the Soviet Union, could gradually pass over to socialism without the Dictatorship of the Proletariat.

<sup>32</sup> Chervenkov, V., *loc. cit.*

<sup>33</sup> Kardelj, *op. cit.*, p. 14.

<sup>34</sup> Gheorghiu-Dej, G., "Consolidating the People's Democracy in Rumania," *For a Lasting Peace, For a People's Democracy*, 1(4), January 1, 1948, p. 4.

<sup>35</sup> Varga, *op. cit.*, p. 3. (See note 13 above).

<sup>36</sup> *Ibid.*, p. 8.

<sup>37</sup> Chervenkov, V. "Under the Banner of Criticism," *For a Lasting Peace, For a People's Democracy*, 15(18), August 1, 1948, p. 3.

It was no surprise to hear President Benes of Czechoslovakia proclaim:

... a mature society, like that of Czechoslovakia, need not go through the Dictatorship of the Proletariat in order to accept socialism. . . . The Soviet Union . . . acknowledges today that the transformation of liberal democracy to its higher degree—to a socializing democracy—should and can come about gradually. . . .<sup>38</sup>

On the other hand, it was a little strange perhaps to hear such communist stalwarts as Gottwald proclaim that the "Dictatorship of the Proletariat is not the only road to Socialism . . . it is possible to move in the direction of Socialism in our own Czech way without the Dictatorship of the Proletariat,"<sup>39</sup> or further to hear Gcmulka of Poland affirm:

We have chosen our own Polish road of development which we have named that of People's Democracy. Along this road and under such conditions, the dictatorship of the working class and even in greater measure the dictatorship of a single party is neither essential nor purposeful.<sup>40</sup>

There was, however, one discordant note struck in this otherwise harmonious chorus of proclamations about the special road to socialism. Yugoslavia, perhaps one of the most advanced of the countries from the point of view of communist control of power, refused to go along with such a theory. While caution was the keynote in the other countries, Tito was beating the drums for the capture of power by the Communists in all of Europe. While the economic changes in the other People's Democracies were being handled with kid gloves, Tito went to the extreme of embarking on a five-year plan for the industrialization of Yugoslavia that even went beyond the Soviet first five-year plan. While the attitude in the other countries was that of harmony with the peasant, Tito embarked on a policy hostile to the peasant.<sup>41</sup> While the other countries were all singing hymns of praise to the special type of democracy and to the movement towards socialism minus the dictatorship

<sup>38</sup> Sharp, *op. cit.*, p. 10.

<sup>39</sup> *Ibid.*

<sup>40</sup> Zaleski, W. *The Pattern of Life in Poland: IX The Party System*, Paris (Mid-European Center), July, 1952, p. 12.

<sup>41</sup> Borkenau, *op. cit.*, pp. 504-05.



of the proletariat, the leaders of Yugoslavia strongly denied that the new democracy was actually "an old parliamentary democratic form with a new substance." As Edward Kardelj insisted:

What is characteristic for the development of People's Democracy in Yugoslavia is precisely the fact that it did not develop along lines of bourgeois parliamentary democracy. . . . People's Democracy in Yugoslavia . . . is actually a specific form of Soviet Democracy which corresponds to our conditions. . . .<sup>42</sup>

These words were a portent of things to come. They were soon to be heard in the other countries.

The picture that emerged from the statements of the Eastern European and Soviet Communists alike was one of moderation in all things, or at least the preaching of moderation. Strenuous efforts were made to deny the value of the Soviet development as a pattern for the development in these countries. At the beginning, many of the theorists proclaimed the similarity of the People's Democracies to bourgeois democracy. This soon changed to an affirmation that the People's Democracies were a new, unique form of democracy, hitherto unknown, being neither socialist nor capitalist, but harmoniously including both types of economy within their societies. The theorists then went on to testify that the People's Democracies were proceeding along an independent path of development. And finally, they conceived of the possibility that the countries might each go on to the path of transition from capitalism to socialism by toning down the class struggle, and by avoiding the need for a dictatorship of the proletariat.

Along with this theoretical picture, however, there also emerged a picture of reality, a picture which indeed testified to moderation during this first phase of totalitarian development in most of the satellite countries, but which also testified to the constant and ever growing accretion of power by the Communists.

*The Instruments of Power.* Despite their doctrine of moderation, the Communists from the very beginning set for them-

<sup>42</sup> Kardelj, Edward. "The Communist Party of Yugoslavia in the Struggle for the Independence of the Yugoslav Peoples, for the People's Power, for the Economic Rehabilitation and Social Reconstruction of the Economy," *For a Lasting Peace, For a People's Democracy*, 1, November 10, 1947, p. 5.



selves the immediate task of gaining control of the instruments of power. The instruments may generally be classified into six general categories: the resistance movements, the trade unions, voluntary associations, the armed forces, key government ministries, and the machinery of land reform and nationalization.

The resistance or liberation movements were used by the Communists in several of the countries as the entering wedges in the gaining of power. The best examples of these movements were in Yugoslavia and Albania in which the Communists gained complete supremacy over all the agencies of power by means of their control of the resistance forces.

The trade unions were another key to power. The "strike" became a crucial weapon in the hands of the Communists.<sup>43</sup> The "mass demonstrations of the working masses" at crucial moments, such as the demonstrations against the Rumanian Radescu government in 1945, or during the Prague coup in February, 1948, demonstrated the effectiveness of this agency of power. Almost from the very beginning, the trade unions in all the countries became dominated by the Communists.

Voluntary associations such as youth groups, women's leagues, veterans' organizations, farmers' unions and consumer cooperatives also became objects of communist infiltration. In Czechoslovakia, for example, the Union of Czech Youth, the Union of Fighters for Freedom, and the United Society of Czech Farmers were all taken over by April, 1946. In Bulgaria, the battle for effective control over the Social Democratic Party was partly decided after the left-wing took over the Social Democratic Cooperative Society. In Poland, the Communists took over the Congress of Peasant Self-help as one of the first steps against Mikolajczyk's Polish Peasant Party.

The army was one of the basic instruments of power. In the ex-enemy countries, Bulgaria, Rumania and Hungary, "the disarmament clauses of the peace treaties made it possible to purge selected officers, leaving behind those most reliable and malleable."<sup>44</sup> Special people's militias, such as the Tudor Vladimirescu unit composed of Rumanian prisoners of war trained

<sup>43</sup> Schoenfeld, H. S. Arthur. "Soviet Imperialism in Hungary," *Foreign Affairs*, April, 1948, p. 560.

<sup>44</sup> Seton-Watson, *op. cit.*, p. 303.

in the Soviet Union, were created.<sup>45</sup> The Minister of Defense in Czechoslovakia, though not a Communist, was a sympathizer of the communist cause and was of great assistance in neutralizing the troops during the Prague coup. Since the Polish army had been almost completely destroyed during the war, the nucleus of the new army was formed from those Polish divisions which had been trained in Russia and had come back to Poland with the Soviet Army. Therefore, although the Minister of War and the Commander-in-Chief were non-party men, the Communists had effective predominance in the army.

Communist predominance in the Ministries of Interior, Justice, Communications and Education assured control of the secret police, the courts and the instruments of propaganda: the press and radio and education. In those countries in which the ministries were not placed in communist hands, either the deputy-minister post was granted to a Communist Party member, such as the Deputy Foreign Minister Clementis in Czechoslovakia, or the post of Minister was given to members of pro-communist parties, such as the Social Democrat Minister of Justice Szakasits and the National Peasant Minister of Interior Erdei in Hungary. Communists were also placed as deputies or key officers in other ministries, so that within a short period of time all the ministries were directly or indirectly supervised by the Communists. As H. S. Arthur Schoenfeld remarked: "By the end of 1946, no Hungarian Ministry or government agency was fully responsive to any non-communist directive without the prior approval from the Communist authority."<sup>46</sup>

In several countries land reform and nationalization were important power instruments. For example, in Hungary, land reform was a vital issue. Command of the Ministry of Agriculture played a key role in the communist rise to power. The Czechoslovakian Ministry of Agriculture was responsible for regulating the border areas in Bohemia from which the Sudetan Germans had been expelled after the war. By its distribution to the peasants of land seized from the Sudetans, the Ministry of Agriculture was able to assure communist ascendancy in

<sup>45</sup> Farberov, *op. cit.*, pp. 182-83.

<sup>46</sup> Schoenfeld, *op. cit.*, p. 562.

those border areas and eventual creation of a communist state within a state.

From the very beginning then, communist control of the key instruments of power, the resistance movements, the trade unions, voluntary associations, the armed forces, key government ministries, and the machinery of land reform and nationalization, assured virtual success to the communist program.

*Destruction of the Old Ruling Class.* Concomitant with the securing of the real positions of power, the Communists in union with the other political parties worked to rid the country of collaborationist elements, fascist leaders and agents, royalists, landlords and big capitalists. One part of this job was the expulsion of the German-speaking minorities in countries such as Rumania and Czechoslovakia, and in accordance with the Kosice program of Czechoslovakia, for example, the confiscation of all property belonging to German-speaking elements who could not prove that they had not actively opposed the German invader during the war. People's Courts were established in order to mete out summary justice to "fascists and collaborators." The trials of the ex-Regents in Bulgaria, the Tiso trial in Slovakia, the spy trials in Albania, and the Mihailovic trial in Yugoslavia were highlights of this procedure.

*Disruption of the Coalition.* With the collaborationist elements and the old ruling classes out of the way, the Communists turned their attention to those parties in the coalition who were competitors or potential competitors for power. The main object was to cast out those competitors from the coalition and restructure the coalition in such a manner as to assure communist control over the remaining parties.

A major obstacle to this consolidation of power at the beginning was the Western powers. It was therefore practical as well as necessary to gain power through the methods of parliamentary democracy in order to avoid giving the Western powers a pretext for interference or intervention. The Western powers had insisted that genuine coalition governments be established in most of the countries after the war. This stipulation had been fulfilled in the cases of Czechoslovakia and Hungary. In Poland and Yugoslavia, where communist-dom-

inated governments had been established prior to the end of the war, the Western powers demanded that the governments-in-exile be represented. In order to avoid premature unpleasantness with the West, Yugoslavia had accepted Subasic, Grol and Sutej into the government, while Poland granted Mikolajczyk's Polish Peasant Party five seats in the government. Albania was the only country which avoided this formality.

In Rumania and Bulgaria, the pattern of events that led to the ousting of the Maniu National Peasants, Bratianu Liberals, Petkov Left-wing Agrarians and the Lulchev Social Democrats occurred so quickly in 1945 that the West was still in a position to insist that these parties be reaccepted into the government. The Rumanian parties were allowed back into the government again, but possessed no real power. Though negotiations were begun with the Bulgarian opposition parties, the attempt ended in failure. All these minor concessions to the West, however, were sufficient to delay any real threat of interference or intervention until it was too late.

The major advantage that the Communists had in their bid for power was the sheer physical proximity of the Soviet Union as well as the presence of the Soviet occupation troops. For the most part, during the first stages of development, most of the moves toward power consolidation by the Communists were self-initiated. Whenever the going became rough, however, especially in the occupied countries, the Soviet authorities were always ready to offer a helping hand to assure communist success.

There will be no attempt in this paper to discuss the historical events in each of the countries in narrative form or chronological order. The stories have been told many times by competent eye witnesses and authorities and require no repetition. What is of importance here is an analysis of the techniques used by the Communists in all the countries in order to accomplish their second goal: driving the opposition out of the government. These techniques were eight in number: Soviet interference, Soviet intervention, infiltration and party-splitting, duplication of parties, hostile communist actions forcing resignations, intimidation and persecution, rigged elections and compromising the opposition.

It should be noted before beginning the analysis of the communist power techniques that a special situation existed in Czechoslovakia. Because of communist popularity and Czech friendship for the Soviet Union, many of the overt acts of power-seeking performed by the Communists in the other countries during the first stage of totalitarian development were delayed in Czechoslovakia until the second stage. Certain events in Czechoslovakia will be discussed in the context of the first stage, however, in order that the Czechoslovak development be compared adequately with the development in the other countries.

The first case of interference by the Soviet Union took place in Rumania in 1944. The first government under General Sanatescu was a government of generals. The leaders of the four coalition parties were only allowed to participate in the government as Ministers without portfolio. In such a position, the Communists were placed at a disadvantage in getting control of the key instruments of power. At this point Soviet General Vinogradov stepped in to protest about the alleged non-fulfillment of armistice terms. The government was forced to resign and Sanatescu formed another government composed of this time of politicians from the four parties.

Bulgaria was the second country to witness Soviet interference. In September, 1944, Dr. G. M. Dimitrov, respected and popular leader of the Left-wing Agrarians, returned from abroad to resume his active role as General Secretary of the Agrarian Union. Though pressed to join the government, he preferred to remain outside and pursue his aim of rebuilding the Agrarian Union. This activity soon brought him into conflict with the Communists and the Soviet Commission. Dimitrov was accused of not only having a close friendship for the West but of even being a British agent. The communist agitation became so great that in January of the next year, at the command of the Soviet General, Dimitrov was forced to resign his post.

The Small Holder Party of Hungary was so powerful that after it received an absolute majority in the Budapest municipal elections, Voroshilov, chairman of the Allied Control Commission, proposed to the leaders of the party that the November, 1945, general election be held on a joint single list of the

four government parties. The Small Holders, encouraged by its victory in Budapest, refused the proposition. The Soviet Union was not one to give up, however, and insisted that regardless of the outcome of the November elections, the coalition continue and participate in the formation of the new government. Despite the fact that the Small Holder party again won an absolute majority in the general elections, it was obliged to participate in a coalition with the other parties. Later in the formation of the government, indirect pressure by the Soviet authorities forced the Small Holders to give the control of the Ministry of Interior to the Communists. Three months later the Soviet Union interfered again by forcing the Small Holders to cast 21 members out of the party on the ground that one of the group, Sulyok, had incurred the wrath of the Soviet authorities by his fervent nationalist speeches. Sulyok soon formed the first opposition group, the Freedom Party.

There was also the suggestion of Soviet interference in Czechoslovakia during the February, 1948, coup, when the Soviet Deputy Minister of Foreign Affairs, Zorin, flew to Prague.

The first major intervention by the Soviet Union was the establishment of the communist-dominated Lublin Committee in Poland as the provisional government.

The second intervention came in Rumania. From December, 1944 until February, 1945, the Communists did their best to create a state of disorder which culminated in a communist-inspired mass demonstration on February 24. Suddenly Soviet troops occupied Rumanian Army Headquarters. Vyshinski flew to Bucharest and demanded of the King that the Radescu government resign and that a new government under Petre Groza of the communist-dominated Ploughman's Front, be formed. On March 6th, Groza became Prime Minister. The Liberal and National Peasant parties were thrown out of the government, their places taken by the Ploughman's Front and the Tartarescu Liberals.

The final example of intervention took place in Hungary. On the pretext of a conspiracy plot implicating the Small Holders, the Communists demanded that the parliamentary immunity of Bela Kovacs, Secretary-General of the Small



Holder Party, be suspended so that he could be interrogated by the secret police. The Small Holder party balked and refused to allow Kovacs to be so compromised. Thereupon the Soviet Union stepped in, exercised its prerogative as the occupation authority and arrested Bela Kovacs for espionage. Kovacs, before he was sent to his death, was forced to implicate the Small Holder Prime Minister, Ference Nagy, in the "conspiracy."

Infiltration and party splitting was the third technique. In Rumania, the Petrescu "right-wing" of the Social Democratic Party broke with the party, resigned its seat in parliament, and went into opposition after the left-wing voted to support a single electoral list at a Party Congress in March, 1946. In May, 1945, after left-wing and communist infiltration, the Bulgarian Left-Wing Agrarians split into the anti-communist Petkov faction and the pro-communist Obbov splinter group, while the Social Democrats divided into the Lulchev anti-communists and the Neikov pro-communists. During the summer of the next year, the Communists split the Zveno party by arresting several members and forcing the Minister of War, Velchev, to resign and accept the post of Minister to Switzerland. In Poland the Mikolajczyk Polish Peasant Party split in a disagreement over the communist-inspired referendum which the Communists had engineered in order to bolster their power.

One of the favorite communist techniques was to create a party which would supposedly represent the same elements of the populace which the potential opposition party represented. As the Soviet Academician Trainin explained: the bourgeoisie, the petty-bourgeoisie, and the peasantry contained two elements, the fascist reactionaries and the radicals. The first group was soon to be found in the opposition, while the second supposedly entered the National Front and took an active role in the "building of a new democratic order."<sup>47</sup> In Rumania, the communist-dominated Ploughman's Front soon took the place of the National Peasant Party, while the Tartarescu Liberals replaced the Bratianu Liberals.

Poland had a more complicated situation. From the very beginning the government-sponsored Peasant Party was in

<sup>47</sup> Trainin, *op. cit.*, I, pp. 9-12.



competition with Mikolajczyk's Polish Peasant Party. Later, after the split of the Polish Peasant Party during the referendum, the splinter group joined with another peasant group, the Piast, to form the Polish Peasant Party—New Liberation. This turn of affairs made the 1947 election a confusing one, and many of the voters who had planned to vote for Mikolajczyk's Polish Peasant Party voted for the other peasant parties by mistake.

Forced resignation was another technique. In August, 1945, the Lulchev Social Democrats and the Petkov Left-Wing Agrarians in Bulgaria resigned after repeated communist intimidation and repression. Dr. G. Dmitrov managed to escape the country. In Czechoslovakia, the ministers representing the Czech National Socialist, Czech Populist, Slovak Freedom and Slovak Democratic parties resigned their posts in February, 1948, in protest over the activities of the Communist Minister of Interior. Mikolajczyk resigned his posts in the Polish government after he had lost in the 1946 referendum. Finally, in Yugoslavia, Grol resigned in August, 1945, and Subasic and Sutej in October after charging that the Communists had not kept their word which had been given when the opposition elements had entered the government in March of that year.

Intimidation and persecution was uniform in all of the countries. Opposition party meetings were broken up by gangs of toughs. Scores were arrested and some leaders were injured or wounded.

Rigged elections was next on the list. The Communists had learned their lesson after the 1945 elections in Hungary. Being self-confident of inevitable victory, they allowed the elections to be free and secret. The result was an overwhelming victory by the Small Holder Party. From then on, the elections in the other countries, except for Czechoslovakia, were held in an atmosphere of intimidation and persecution. Opposition candidates had a difficult time in meeting the qualifications. Obstacles of all sorts were placed in the way of registration for voters supporting opposition candidates. The repression was so great in Bulgaria and Yugoslavia that the opposition decided not to participate in the elections in order to avoid terrorization of the populace. In most of these

later elections, the communist-controlled bloc won an overwhelming majority of the votes and parliamentary seats.

The first attempt at compromising the opposition came in Rumania in August, 1945, when the Minister of Interior announced the discovery of two terrorist organizations which were planning the overthrow of the government and the assassination of its members. Followers of Maniu and Bratianu were implicated. The remarkable success of this technique so encouraged the Communists that from then on, in every country the charges of conspiracy and later of espionage by a foreign power were used as trump cards by the Communists.

Dmitrov of Bulgaria was accused of being a Western agent and Petkov was implicated in an alleged conspiracy. Members of the Small Holder Party in Hungary were implicated in the shooting of several Red Army officers as well as some anti-semitic riots. Later these charges in turn were enlarged into conspiracy and espionage, bringing Bela Kovacs to prison and death, and finally forcing the resignation of Prime Minister Nagy and his replacement by the collaborationist rump-wing Small Holder, Dinnyes.

In Czechoslovakia, the Slovak Democrats, the chief threat to the Communists in Slovakia, were implicated in a "Slovak Terrorist Plot" and hundreds upon hundreds of "Slovak Fascists" and members of "Tiso detachments" were arrested. In Poland, Mikolajczyk, himself, was incriminated as an agent of the Western powers and a tool of reactionary generals, landlords and capitalists.

Thus it can be seen how successful the Communists were in driving the major contenders for power into opposition and preserving a communist-controlled coalition. By the techniques of Soviet interference, Soviet intervention, infiltration and party splitting, duplication of parties, actions provoking resignations, intimidation and persecution, rigged elections and compromising the opposition, their goal was achieved.

The People's Democracies were soon to come to the end of the first stage of totalitarian development. The embryos of the second stage were already clearly seen in the early years of the countries' existence. Yugoslavia and Albania were already monolithic states. The premature ousting of the opposition parties of Rumania and Bulgaria already in 1945, and the

movements against Mikolajczyk in Poland and the Small Holders in Hungary were tell-tale portents of the events to come. The implicating of the various opposition parties in alleged conspiracies pointed to a perilous future for the non-communist elements in each of the countries.

#### THE SECOND STAGE: TIGHTENING-UP

The second stage of totalitarian development lasted from the middle of 1947 until the middle of 1948. The key event which marked the beginning of this period was the initiation of the Marshall Plan by the United States in July, 1947. It is a well-known fact that both the communist-controlled government of Poland and the communist-infiltrated government of Czechoslovakia had strongly desired to participate in the preparatory conference in Paris which finally drafted the provisions of the Marshall Plan agreement. The years of moderation and semi-independence had gone to the heads of the local Communists. Stalin immediately summoned the Czech and Polish leaders to Moscow and laid down the law that they were not to participate in the Western conference or accept Marshall Plan aid. To make this bitter pill easier to swallow, the Soviet Union immediately offered a trade treaty to Czechoslovakia. The reaction in Czechoslovakia was immediate. The non-communist parties, still wielding power in the government, indicated their great discontent with this turn of affairs. From here on, the patterns of independence in each of the countries were gradually obliterated and the Soviet Union began to tighten its reigns. There was now a sudden movement toward uniformity as the relations between East and West deteriorated.

*People's Democracy: The Soviet Union as a Model.* Signs of a new interpretation of People's Democracy were observed. The slogans of an "independent road to socialism" or a "specific Polish or Bulgarian path of development" were significantly narrowed in their interpretation. As Samuel Sharp pointed out:

The specific nature of the development in Eastern Europe was now regarded merely as meaning that favorable conditions created by the war (particularly the victory of the Soviet Union and the collapse of the pre-war ruling groups in Eastern Europe) removed

the need for the establishment of an exclusive Dictatorship of the Proletariat. . . .<sup>48</sup>

In September, 1947, the representatives of nine Communist parties, Yugoslavia, Bulgaria, Rumania, Hungary, Poland, the Soviet Union, France, Czechoslovakia and Italy met in Poland to establish the Cominform, the successor to the Comintern.<sup>49</sup> The keynote speech of Zhdanov of the Soviet Union emphasized the division of the world into the Western imperialist camp and the Eastern peace-loving, democratic camp. There was now no room left for a third force. From here on the emphasis on the differences between the development of the Soviet Union and the development of the People's Democracies began to be considerably toned down.

The Soviet theorist, A. Leontiev, provided the perfect transition for this new phase of satellite development. He strongly maintained that the development toward socialism in these countries was not an independent one, but was only possible because socialism had been victorious in the Soviet Union. Only now could a new, previously non-existent opportunity for the smaller nations be possible. The building of socialism in one country on an independent basis only applied to the Soviet Union and not to the smaller countries.<sup>50</sup>

Soon the leaders of the satellite countries picked up the cue. Hilary Minc of Poland took issue with his comrade, Bierut, who previously had stressed the specific harmony of the capitalist and socialist elements in the Polish economy. Minc affirmed that "any attempt to compromise with capitalist elements . . . must inevitably lead to the return of capitalism."<sup>51</sup> He went on to criticize those who had desired a middle way between capitalism and socialism. Although he admittedly emphasized that the transition to socialism in Poland as well as in the other countries was taking place in a special way, that each country's development was different according to its particular national, social, economic, political and historical peculiarities, he never-

<sup>48</sup> Sharp, *op. cit.*, p. 14.

<sup>49</sup> *For a Lasting Peace, For a People's Democracy*, "Communiqué on the Informative Conference of Representatives of a Number of Communist Parties, 1, November 10, 1947, p. 1.

<sup>50</sup> Leontiev, *op. cit.*, p. 70.

<sup>51</sup> Minc, H. "From a People's Democratic Poland to a Socialist Poland," *For a Lasting Peace, For a People's Democracy*, 15(18), August 1, 1948, p. 2.

theless affirmed that the experience of building socialism in the Soviet Union had been of world historical significance and served as an example to all peoples.<sup>52</sup>

Several weeks later, Bierut himself decried the "opportunist tendency of avoiding the class struggle" and went on further to say that although there were certain specific features in the Polish path to Socialism, it was not "something qualitatively different from the general path of development toward socialism," but differed "only in form from the general path of development."<sup>53</sup> The difference was attributed to the fact that there had been a preliminary victory of socialism in the Soviet Union.

The President of the Bulgarian Academy of Sciences, Professor Pavlov, summed up the essence of the People's Democracies by stating that while every people imparted its own traits to the building of socialism, "the path taken by the Soviet Union is in essentials the same for all countries which are advancing or will advance toward Socialism."<sup>54</sup> The Soviet experiment was now to be the model for the other countries.

*Destruction of the Opposition.* Along with the tightening up in the theoretical sphere, a new development became apparent on the political scene during the second stage of totalitarian development. Coincident with the announcement by the West of the Marshall Plan, the Communists in Eastern Europe turned from a policy of limiting the powers of the opposition parties to a policy of destroying every vestige of such opposition. Leaders of the opposition parties either fled the country or were arrested. In most of the countries, a series of political trials were held in which the opposition leaders were found guilty of espionage and executed. The remnants of the opposition parties were either dissolved or thoroughly communized.

The example set by Dimitrov of Bulgaria in his flight to freedom in December, 1945 was soon to be followed. Only the fortunate few, Pfeiffer and Barankovits, leaders of two Hungarian Small Holder splinter groups, Imre Kovacs of the

<sup>52</sup> *Ibid.*

<sup>53</sup> Bierut, B. "For the Complete Elimination of the Right and Nationalist Deviation," *For a Lasting Peace, For a People's Democracy*, 18(21), September 15, 1948, p. 3.

<sup>54</sup> Pavlov, "Participation of the Intelligentsia in the Development of People's Democracy in Bulgaria," *For a Lasting Peace, For a People's Democracy*, 15(18), August 1, 1948, p. 5.

Hungarian National Peasant Party and Mikolajczyk of Poland were able to escape and follow Dmitrov's path to freedom. Others such as Masaryk and Benes of Czechoslovakia found their escape through suicide and natural death. The others, Maniu and Bratianu of Rumania, Petkov and Lulchev of Bulgaria, the leaders of the National Socialist, Populist, Freedom and Democratic Parties of Czechoslovakia, Jovanovic and others in Yugoslavia and Albania, were arrested.

In Rumania and Bulgaria, the opposition party leaders were brought to trial and charged with conspiracy to overthrow the government with the aid of the United States and Great Britain. All were found guilty and either executed, as Petkov, or sentenced to long terms in prison.

In Rumania the National Peasant Party, the Bratianu Liberals and the Petrescu Social Democrats were dissolved before the end of 1947. Similarly the Bulgarian opposition parties, Petkov's Left-Wing Agrarians, Lulchev's Social Democrats, and Mushanov's Democrats were dissolved following the trials of each of the leaders.

Hungary had a more complicated situation. There, following the resignation of Nagy, the majority of the Small Holders went into opposition, divided into four opposition groups: Father Balogh's Independent Democratic Party, Barankovits' Catholic Democratic People's Party, Pfeiffer's Hungarian Independent Party, and Schlachta's League of Christian Women. The remaining Small Holders became part of the government coalition. Following the August, 1947 elections, where the opposition parties managed to get a surprisingly large vote (39 per cent),<sup>55</sup> the Communists began to attack each of the parties in turn. After the charge of conspiracy against Pfeiffer and his flight abroad, all 49 members of his parliamentary party were deprived of their seats. In the same month the four seats of Schlachta's League of Christian Women and some of the Barankovits' party seats were taken away. After the arrest of Cardinal Mindczenty, Barankovits' Catholic Democratic People's Party was also dissolved. Balogh's Independent Democrats joined the government electoral bloc in April, 1949. In the meantime, the National

<sup>55</sup> Betts, R. R., ed. *Central and South East Europe, 1945-1948*, London, 1950, p. 116.



Peasant Party had been purged several times and by 1948 ceased to be an independent organ, but like its counterpart in Rumania, the Ploughman's Front, became the rural branch of the Communist Party.

The conspiracies, plots, intimidations, and arrests of opposition elements, delayed until now in Czechoslovakia, suddenly burst forth after the announcement of the Marshall Plan. The Slovak Democrats were the first to be hit, being implicated in a "Slovak Terrorist Plot." Soon they lost their majority on the Slovak Council of Trustees. Finally in February, after the resignation of "opposition" party ministers, the Communists succeeded in a *coup d'état* and became the masters of the country. Following the arrests of the opposition leaders, the Communists dissolved the Slovak Democratic Party and appointed individuals known to be loyal to them to the leadership of the other non-communist rump parties.

In Poland, the Communists had taken over the Labor Party as early as August, 1946. Following the flight of Mikolajczyk, the remaining remnant of his Polish Peasant Party was admitted to the government bloc along with the Polish Peasant Party—New Liberation. Opposition in all countries had been destroyed.

*The Purge of the Coalition.* Coincident with the establishment of the Cominform in September, 1947, the Communists turned their attention to the purging of all dissident elements remaining in the government coalitions. The theoretical rationalization for the move was that in states of the People's Democracy, there could be at most only one party representing the classes of society: the bourgeoisie and liberals, the peasants and the workers.<sup>66</sup> Action was taken against each group of "class" parties in turn. Parties were either communized, dissolved or purged of "right-wing" elements and united with other parties representing the same class. The National Front was then thoroughly rehailed and became a complete instrument of the Communist Party.

The first government coalition party in Rumania to feel the new policy of the Communists was the Tartarescu Liberals.

<sup>66</sup> Nowak, Antoni. *The Pattern of Life in Poland: I. Preliminary Notes on Political Institutions of Poland*. Paris (Mid-European Center), February, 1952, p. 16.



Following a vote of no confidence, Tartaescu and other Ministers were forced to resign their posts and the party was dissolved. Two other parties, the National Popular Party and the Hungarian People's Union, which had been in existence for only a short while, were well controlled by the Communists and became a part of the new government coalition and National Front.

In Bulgaria, the remnants of the Zveno and Radical parties were eliminated by January, 1949, while the Balogh Independent Democrats of Hungary became members of the communist coalition.

In Czechoslovakia, the purged rump opposition parties became a part of the new monolithic coalition. The Polish Democratic party had been a communist front party from the very beginning.

In January, 1948, the remnants of the National Peasant Party were merged with the Ploughman's Front to form a United Peasant Party in Rumania. The Obbov remnants of the Left-Wing Agrarians remained to represent the Peasants in Bulgaria.

The Communists moved again against the remains of the Rump Small Holder Party in Hungary. The Small Holder President of the Republic, Tildy, was forced to resign. Soon to follow was the collaborationist Prime Minister, Dinnyes. Dobi, an even more subservient Small Holder, took Dinnyes' place and the Rump Small Holder Party came completely under Communist control.

Finally in Poland, the left-wing of the Polish Peasant Party, the Polish Peasant Party—New Liberation, and the original government-sponsored Peasant Party merged into a United Peasant Party.

The plight of the socialist parties was dramatically portrayed in Poland. The Polish Socialist Party had been the stronghold of the original theories about People's Democracies. The "third way" theory greatly appealed to it. The Socialist Party considered that it had something unique to offer to the future development of Poland. It contended that even under socialism, the existence of two parties representing the workers would be valuable. Finally when the question of amalgamation

with the Communists arose, the Socialist Party firmly believed that

. . . the basis for amalgamation of the parties must be a new ideology, representing a synthesis of the elements of freedom allegedly inherent in the Social Democratic Party and the elements of revolution characteristic of the Communist Party.<sup>87</sup>

Naturally the Communists rejected such a notion. In any alliance, the Communists were to have the leading role.

In Rumania and Bulgaria, the Social Democrats had been purged long ago, all that was left was to convince the parties of the wisdom of fusion with the Communists. Finally, the decision was made to form a United Workers' Party in Rumania and a United Communist Party in Bulgaria.

Hungary, Czechoslovakia and Poland presented more difficult problems. Not only did the Communists have a difficult time in convincing the socialist parties that fusion was the only path for them to follow, but after the decision for fusion had been made, each of the socialist parties had to purge the right-wing (anti-fusion) elements before the Communists finally allowed the fusion to take place. In Czechoslovakia, while the Czech Social Democrats were allowed to fuse with the Communists, the Slovak Social Democrats were forced to disband with a stipulation that the members were permitted to join the Communist Party. The Slovak Communist Party had long ago become one with the Czech Communists.

The parties remaining in each country after the purge of the government coalitions were the United Communist or Workers' Parties, the United Peasant Parties, except in industrial Czechoslovakia, and the various "bourgeois" or "liberal" remnants still existing in several of the countries. It should be noted that in Yugoslavia and Albania, the purging of the National Front and government coalition had taken place during the first few years of the post-war period.

It has been seen that in the second stage of totalitarian development, Moscow began to strengthen its hold on the satellite countries. The events in each country began to take

<sup>87</sup> Farberov, N. P. "On Classes and Parties in the Countries of People's Democracy of Central and South East Europe." Condensed from *Sovetskoe Gosudarstvo i Pravo* 9, 1949, 8-22, in the *Current Digest of the Soviet Press*, II:4, 1950, p. 4.

on a more uniform appearance. During this period every last vestige of opposition and every dissident element within the government coalition were destroyed. The communist consolidation of power was nearing its end.

#### THE THIRD STAGE: UNIFORMITY

With the second stage of totalitarian development coming to a close, the third stage burst onto the scene with dramatic suddenness in June, 1948 when the Cominform expelled Yugoslavia from its ranks.

The main reason behind the Cominform resolution was that Tito and the Yugoslav Party had dared to be independent. Though they had been loyal servants to the cause of international communism and avid worshippers of the Soviet Union, the Yugoslavs demanded to have control over their own country, to have complete independence in their policies. As Tito proclaimed in 1945: "We demand that everyone shall be master in his own house; we do not want to pay for others; we do not want to be used as bribes in international bargaining. . . ." <sup>88</sup> In 1947-48, when international events forced the Soviet Union to begin a policy of tightening control over the satellite countries, the Yugoslav attitude proved a dangerous stumbling block.

The consequences of the break with Tito were immediate. If Yugoslavia had been guilty of independence and nationalism at the expense of concessions to the Soviet Union, then the germs of Titoism were also present in the other satellite countries. Had not the local Communists been preaching national unity and moderation for two years? Had not the tempo of events from 1945-47 been primarily initiated by the local Communists and not Moscow? Is it any wonder then that the local Communists themselves had been taken in by their own line? Is it any wonder that they believed that the goal of the dictatorship of the proletariat was something to be achieved not now but in the future? Certainly, the blatant willingness of the Czech and Polish Communist Parties to participate in the Marshall Plan was an indication of too much independence and of too much nationalism. Even though the old line of moderation and national development was merely a communist tactic

<sup>88</sup> Raditsa, *op. cit.*, p. 124.

to gain time and power, nevertheless, it contained elements which obviously were genuinely attractive, even to the various Communists in leading positions. The Hungarian, Josef Revai, had certainly admitted that the communist line from 1945-47 was a mere facade. "It was correct not to show our cards," he had confessed. At the same time, however, he admitted that even the Communists themselves had forgotten "that the People's Democracy . . . was more than just a plebeian victory of the bourgeois democracy and that it was a step toward the Socialist transition, which contained even then the elements of development into the Dictatorship of the Proletariat."<sup>59</sup>

*People's Democracy: A Form of the Dictatorship of the Proletariat.* The Tito affair was the decisive factor in the communist "new look" policy. The process of tightening up, of establishing the lines of uniformity, begun after the Marshall Plan and formalized with the creation of the Cominform, was now suddenly intensified. There was to be no more foolish talk of moderation, of individual paths to socialism, of independent developments. There was to be no more "master in his own house." The satellite attitude toward the Soviet Union was now elevated to the point where it became an essential and decisive factor affecting the very nature of the Eastern European regimes. Dmitrov, the leading Communist in Bulgaria, contended that "any tendency toward a weakening of cooperation with the U.S.S.R. is directed against the very foundations of the People's Democracy in our country."<sup>60</sup>

A corollary argument to Dmitrov's was the statement of Gheorghiu-Dej in Rumania that "any underestimation of the role of the Soviet Union and the People's Democracies in Eastern Europe is a dangerous nationalist phenomenon and inevitably leads to the departure from the position of Marxism to that of capitalism."<sup>61</sup>

Kolarov of Bulgaria even went so far as to lay down a type of criterion for security and loyalty clearance: "The demarca-

<sup>59</sup> Revai, *op. cit.*, p. 148.

<sup>60</sup> Dmitrov, G. M. "Report to the Fifth Congress of the Bulgarian Workers' Party" (Communist), *For a Lasting Peace, For a People's Democracy*, December 18-25, 1948, 1(28), January 1, 1949, p. 3.

<sup>61</sup> Gheorghiu-Dej, G. "Betrayal of Revolutionary Marxism," *For a Lasting Peace, For a People's Democracy*, 13(16), July 1, 1948, p. 3.

tion line, nowadays, that which divides the imperialist and anti-imperialist camps, is precisely the attitude towards the Soviet Union. . . .<sup>62</sup>

The Soviet and satellite theoreticians got busy again. The process of Orwellian "double-think" was put into operation. The time had come to take the Soviet Union from behind the scenes and cast it in the leading role. The previous tributes which had been paid to the Soviet Union for its having "liberated" the peoples of Eastern Europe from the fascist invader were now made into a catechism which had to be repeated over and over again, each spokesman attempting to outshine the other in his zeal and ever-burning appreciation for the Soviet Union and its beloved Red Army.

The theoreticians never ceased proclaiming that only the destruction of fascism by the Soviet Army created the conditions for the victory of the popular revolutions in the People's Democracies;<sup>63</sup> that only the victory of the Soviet Army made it possible for the working masses to come to power.<sup>64</sup> Bierut of Poland insisted that the rise of People's Democracies was a "direct result" of the victory of the Soviet Union over the German invaders.<sup>65</sup>

Furthermore, because the Soviet Army not only destroyed fascism, but also liberated the Eastern European countries, the states were able to establish their dictatorships of the proletariat without the need of going through a civil war, as had the Soviet Union after its revolution.<sup>66</sup> Of course the statement did an injustice to the facts, for certainly in Yugoslavia and Albania, if not in Poland, a civil war had been fought along with the war against the invaders. But such refinement would have perhaps been a bit embarrassing to all concerned. Together with prevention of a civil war, the Soviet Army had also prevented an Anglo-American intervention<sup>67</sup> of the type which had previously occurred in the Soviet Union and which pre-

<sup>62</sup> Kolarov, V. "Struggle against Nationalism in the Bulgarian Communist Party," *For a Lasting Peace, For a People's Democracy*, 10(37), May 15, 1949, p. 2.

<sup>63</sup> Farberov, *op. cit.*, p. 39. (See note 4 above).

<sup>64</sup> Mankovsky, B. S. "Gosudarstvo i Pravo Stran Narodnoi Demokratii," *Teoriya Gosudarstva i Prava*, Moscow, 1949, chapter 16, p. 455.

<sup>65</sup> Bierut, B. "Ideological Basis of the United Workers' Party of Poland," *For a Lasting Peace, For a People's Democracy*, 1(28), January 1, 1949, p. 2.

<sup>66</sup> Georgescu, T. "Political Foundations of the People's Democratic System," *For a Lasting Peace, For a People's Democracy*, 11(38), June 1, 1949, p. 4.

<sup>67</sup> Mankovsky, *op. cit.*, p. 455; Farberov, *op. cit.*, p. 13. (See note 4 above)

vented a successful revolution in Greece.<sup>68</sup> Therefore, the People's Democracies did not have to go through the painful period of War Communism as did the Soviet Union.

These statements were not enough, however. The theory of liberation by the Soviet Army even had to be extended to the countries of Yugoslavia and Albania. While the previous statements of Soviet liberation had always excepted Yugoslavia and Albania and had in fact eulogized the brave resistance of the Yugoslav Partisans, now the new theory had to take these countries into account. Gheorghiu-Dej criticized the Yugoslavs for never having mentioned the fact that the victory of the Partisan movement in Yugoslavia would have been impossible without the direct assistance of the Soviet Army. "At a critical period of the National Liberation struggle in Yugoslavia, the Soviet Army liberated Belgrade, thus making Anglo-American imperialist intervention impossible. . . ." <sup>69</sup> Surely no one would deny that the Soviet troops entered Yugoslavia, but surely one could deny that the Soviet troops were responsible for Yugoslavia's liberation. But the pressure was on, and Yugoslavia had to be the scapegoat.

The crowning distortion, however, came when Enver Hoxha of Albania perjured himself to the extent of asserting that the Soviet Union was the "creator" of the People's Democracy in Albania and the Soviet Army its liberator. "Without the Soviet Union . . . the establishment in our country of the People's Democratic system would have been out of the question. . . . The People's Republic of Albania owes its existence to the glorious Soviet Union and its army." <sup>70</sup>

As a second thesis in the new policy, the doctrine that the Soviet Union was not a model for the development of other countries was now completely abolished. The Soviet theorist, Farberov, rejected the theory of "the special road to socialism":

The very assertion of the possibility of building socialism exclusively by a country's own forces and in its own special way, when a country of victorious socialism . . . [exists] . . . is a pure incarnation of nationalism which was and remains the mortal enemy of socialism. <sup>71</sup>

<sup>68</sup> Farberov, N. P. *Konstitutsii Stran Narodnoi Demokratii*, Moscow, 1949, p. 3.

<sup>69</sup> Gheorghiu-Dej, G. "Betrayal of Revolutionary Marxism," *For a Lasting Peace, For a People's Democracy*, 13(16), July 1, 1948, p. 3.

<sup>70</sup> Hoxha, Enver, "Success of the Albanian People's Republic," *For a Lasting Peace, For a People's Democracy*, 32(59), August 11, 1950, p. 4.

<sup>71</sup> Farberov, *op. cit.*, p. 4. (See note 57 above.)



To be sure, the different historical development of each country as well as its own peculiar national characteristics, accounted "for a certain diversity in the forms of their advance to socialism," the Rumanian Georgescu had to admit, but

... any attempt to exaggerate the importance of the specific features of each individual country represents in itself an opportunist and nationalist tendency, which in essence leads to a rejection of the Marxism-Leninism and its basic content the Dictatorship of the Proletariat.<sup>72</sup>

Bierut actually attributed the specific national diversities and different historical developments of the various countries to the fact that the People's Democracies "came into being with the help and support of the Soviet Union."<sup>73</sup>

At this point a confession, a recantation and a compliment to the Soviet Union had to be made to soothe the feelings of Moscow. Josef Revai admitted that during the struggle for power, the members of the party had not been aware of the great change which had occurred in the country and the direction toward which the country was going. Thanks to the decisive assistance received from the Communist Party of the Soviet Union and to the personal aid and teaching of Comrade Stalin, however, the Hungarian party had been able to clarify its future development and expose the dangerous right and nationalist deviationists among them.<sup>74</sup> It now became clear that the "indispensable" condition for the development of the People's Democracies was the experience of the Soviet Communist Party and the experience of socialist construction in the Soviet Union.<sup>75</sup> Gomulka, himself accused of deviation in Poland, recanted his previous ideas by saying that "... not a single country of the new democracies can secure its independence and sovereignty, can develop and advance toward socialism, without the closest cooperation with the Soviet Union."<sup>76</sup>

Of what use was the experience of the Soviet Union to be

<sup>72</sup> Georgescu, T., *loc. cit.*, note 66 above.

<sup>73</sup> Bierut, B., *loc. cit.*, note 65 above.

<sup>74</sup> Revai, *op. cit.*, p. 147; cf. also Farberov, N. P., *op. cit.*, p. 5 (see note 68 above).

<sup>75</sup> Farberov, *op. cit.*, p. 27 (see note 4 above); *For a Lasting Peace, op. cit.*, Zawadski, A. "Alliance with the U.S.S.R.—the Basis of Social Development in the People's Democracies," 25(52), November 4, 1949, p. 2.

<sup>76</sup> Gomulka, W. "Speech at the Active of the Polish Workers' Party," *For a Lasting Peace, For a People's Democracy*, 18(21), September 15, 1948, p. 4.



put in the satellite countries? How had the support and the aid from the Soviet Union helped in the development of these countries? The theorists explained that the first advantage derived from the Soviet Union was that the Communists were able to create their state apparatus much more rapidly and under much more favorable circumstances than had been the case when the Bolsheviks came to power in Russia.<sup>77</sup> Despite the official denials of Soviet interference in the internal affairs of the Eastern European countries during the first few years after the war, the time had now come to admit the facts, for the purpose was to destroy every last vestige of independence within the satellite countries. The claim was made, furthermore, that the many-sided help of the Soviet Union had allowed the satellite countries to lay the foundations and begin the construction of socialism in a much more rapid manner<sup>78</sup> and under incomparably more favorable conditions than those which faced the Soviet Union during the initial period of socialist construction.<sup>79</sup> The People's Democracies were in a position to avoid many of the difficulties which the Soviet Union had faced. It followed from all this that the "economic-organizational and cultural-educational functions" were to have much greater importance, "even in the first phase of the development of the People's Democracies, than they had during the same phase of the USSR's development."<sup>80</sup> This statement was in reference to Stalin's formulation of the three functions of a Socialist state: (1) destruction of the exploiting classes within the state, (2) defense of the country against external attack, and (3) economic-organizational and cultural-educational functions.<sup>81</sup>

According to the Stalinist theory, the economic-organizational and cultural-educational functions became important in the Soviet Union only in 1936 after the victory of socialism had been achieved and the state entered on the transition from

<sup>77</sup> In the Institute of Law of the Academy of Sciences, U.S.S.R. "Problems of State and Law in the Countries of People's Democracy," translated from *Sovetskoe Gosudarstvo i Pravo*, 5, 1949, 64-70, in the *Current Digest of the Soviet Press*, 1:33, 1949, p. 11.

<sup>78</sup> Mankovsky, *op. cit.*, p. 466.

<sup>79</sup> Rautu, L., "Ideological and Political Education of Communists," *For a Lasting Peace, For a People's Democracy*, 20(47), September 1, 1949, p. 3.

<sup>80</sup> In the Institute of Law of the Academy of Sciences, *op. cit.*, p. 11.

<sup>81</sup> Mankovsky, *op. cit.*, p. 464.

socialism to communism, whereas these specific functions were of key importance in the satellite countries even in the first phase of development, from capitalism to socialism. Here was the theoretical justification for the development in the satellites, a development which had been telescoped, thanks to the presence, support and aid of the Soviet Union.

The final element in the establishment of a new theory to rationalize the post-Tito situation was the new attempt to redefine the essence of People's Democracy. The old theories of a "Democracy of a new or special type, being neither capitalist nor socialist," had to be rethought.

The first theoretician to blaze the new path to a revised theory was E. S. Lazutkin. At a conference of economists in 1948, Lazutkin criticized the theory of Varga on "Democracy of a new type." He ended by agreeing that People's Democracy had its special characteristics, but such characteristics in no way changed the fact that "People's Democracy is of the same type as the Soviet government: both the Soviet government and People's Democracy are forms of the Dictatorship of the Proletariat."<sup>82</sup> The satellite leaders were soon to respond. G. Dmitrov in his oft-quoted speech to the Fifth Congress of the Bulgarian Worker's Party restated the Lazutkin thesis: "According to Marxism-Leninism, both People's Democracy and the Soviet system are two forms of one and the same power: the power of the working class in alliance with the working people which it is guiding. . . ."<sup>83</sup> Despite the fact that there was a special form of the transition from capitalism to socialism in Bulgaria, the laws governing the transition were "common to all forms." Only under the dictatorship of the proletariat could such a transition take place. In effect, the People's Democracies were fulfilling the functions of the dictatorship of the proletariat.

The Dmitrov speech caused a sudden spurt of activity by the theoreticians. Quotations were dug up from the master theoreticians of communism, Marx, Engels, Lenin and Stalin, to prove that the People's Democracies were nothing other than a form of the dictatorship of the proletariat. Favorite

<sup>82</sup> Lazutkin, E. S., "Speech" in *Voprosy Ekonomiki*, 9, 1948, p. 106.

<sup>83</sup> Dmitrov, V., *loc. cit.*, note 60 above.

among the quotations was the one from Marx's *Critique of the Gotha Program*:

Between capitalist and communist society lies the period of the revolutionary transformation of the one into the other. There corresponds to this also a political transition period in which the state can be nothing but the *revolutionary dictatorship of the proletariat*.<sup>84</sup>

It seemed strange that the theoreticians had not thought of this idea before. But the times had been different and had called for moderation until power had been obtained. Revai admitted the mistakes of the Hungarian Party:

. . . we concluded from the popular, and therefore relatively peaceful, character of the development into Socialism, that we could achieve Socialism without a Dictatorship of the Proletariat . . . [or] that we needed the Dictatorship of the Proletariat for the achievement of Socialism, but considered the Dictatorship of the Proletariat as a form of government which should follow the People's Democracy, and therefore did not consider the People's Democracy a characteristic form of the Dictatorship of the Proletariat.<sup>85</sup>

From the thesis that the People's Democracy was a specific form of the dictatorship of the proletariat, it was only a short step to contending that the People's Democracies were states of a socialist type because they had set themselves the task of going over to the path of socialism.<sup>86</sup> The Soviet theoretician, Farberov, explained it in this way: the term socialist state meant two things, first, a state building socialism, a state which was socialist in aims, or second, a state of victorious socialism, a state which was socialist in fact.<sup>87</sup> The only difference between the two forms was that the first was in the transition from capitalism to socialism and the second was in the transition from socialism to communism.<sup>88</sup> The proper formula for the essence of the People's Democracies was therefore the following:

<sup>84</sup> Marx, K. "Critique of the Gotha Program," *Selected Works*, Vol. II, New York, n.d., p. 577; cf. Farberov, *op. cit.*, p. 24 (see note 4 above).

<sup>85</sup> Revai, *op. cit.*, p. 148.

<sup>86</sup> Minc, H. "Concerning the Basis of Planning in the People's Democracies," *For a Lasting Peace, For a People's Democracy*, 27(54), November 18, 1949, p. 2.

<sup>87</sup> Farberov, *op. cit.*, p. 27 (see note 4 above).

<sup>88</sup> *Ibid.*, p. 31.

A People's Democratic state = a state building socialism = a proletarian state = a state of the socialist type.<sup>89</sup>

The main difference between the Soviet and People's Democratic states was the fact that the one had already been victorious in socialism while the other was still in the process of building socialism. Another difference which Rakosi of Hungary noted was that the People's Democracy was a dictatorship of the proletariat, "though not in Soviet form."<sup>90</sup> The reason for the fact that the satellites were able to move onto the path of socialism without the Soviet form was because, as Dmitrov pointed out, these countries had been in close cooperation and had received support and aid from the Soviet Union.<sup>91</sup> It was of course admitted that the Soviet Union had a much higher form of the dictatorship of the proletariat,<sup>92</sup> and that it had attained a higher level of "democracy."<sup>93</sup>

Another quotation of Marx from the *Critique of the Gotha Program* about the new state still having the "birthmarks of the old society" was brought out to explain why the People's Democracies had not reached such a high form of development.<sup>94</sup> "Our state . . . is still wearing the eggshells of its origin, remnants from the period of the bourgeois democratic transformation. . . ." Josef Revai said.<sup>95</sup> Revai further called for Hungary to come closer to the Soviet-type of state, while Georgescu of Rumania was already declaring that "the establishment of People's Councils signify that in form the People's Democracy is approaching the higher form of the dictatorship of the proletariat."<sup>96</sup>

A third main difference between the Soviet Union and the People's Democracies was that while in the Soviet Union there existed only one party, in the People's Democracies a multi-party system existed.<sup>97</sup> Firm assurances were given, however, that though the government bloc was composed of several parties, it was the working class alone which was in power; it

<sup>89</sup> *Ibid.*, p. 24.

<sup>90</sup> Revai, *op. cit.*, p. 144.

<sup>91</sup> Dmitrov, V., *loc. cit.*, note 60 above.

<sup>92</sup> Gheorghiu-Dej, G., *loc. cit.*, note 66 above.

<sup>93</sup> In the Institute of Law of the Academy of Sciences, *op. cit.*, p. 15.

<sup>94</sup> Marx, *op. cit.*, p. 563.

<sup>95</sup> Revai, *op. cit.*, p. 151.

<sup>96</sup> Gheorghiu-Dej, G., *loc. cit.*, note 66 above.

<sup>97</sup> Mankovsky, *op. cit.*, p. 470.

was the Communist Party alone which ran the state machine.<sup>98</sup> The theoreticians further explained that the multiparty system did not constitute an "essential difference" between the Soviet and People's Democratic systems, for with the further consolidation of the People's Democracies the basis for the independent existence of the peasant and other parties was to disappear.<sup>99</sup>

In conclusion, a final touch to the theory was necessary in order to explain the complete development of the People's Democratic regimes from beginning to end. This was done by explaining that the resistance movements during the war had not only solved the problem of national liberation, but had also solved the problem of the "social emancipation of the working people."<sup>100</sup>

Further, an adaptation of Lenin's thesis of two revolutions was applied to explain that the revolution in the People's Democracies was in class essence and motivation a socialist revolution which in the course of its development, "also solved the problems of the bourgeois-democratic revolution."<sup>101</sup>

The circle was now complete. The communist theory of the People's Democracies had turned 180°. The previous denial of the value of the Soviet experiment to the development of the Eastern European countries was discarded. Now the relation between the Soviet and satellite regimes became the essential factor affecting their very nature. The Soviet Union was now hailed as the liberator of Eastern Europe, indeed even the liberator of Yugoslavia and Albania. The Soviet Union was the only force which prevented a civil war, Anglo-American intervention and consequently the phase of War Communism in the People's Democracies. The concept of a special independent road to socialism was obliterated and in its place was erected the new thesis that only with the help and support of the Soviet Union, only by the use of the Soviet experience, could the new regimes attain socialism. The old idea about a new, special type of democracy, about a third form between socialism and capitalism, was no longer in vogue. The People's Democracies

<sup>98</sup> Revai, *op. cit.*, p. 149.

<sup>99</sup> Farberov, *op. cit.*, p. 5 (see note 57 above).

<sup>100</sup> In the All Soviet Law Institute under the U.S.S.R. Ministry of Justice, "Discussion of the Textbook for Higher Education Institutions, 'The State Law of the People's Democracies,'" translated from *Sovetskoe Gosudarstvo i Pravo*, 7, 1950, 77-80, in the *Current Digest of the Soviet Press*, 11:43, p. 11.

<sup>101</sup> In the Institute of Law of the Academy of Sciences, *op. cit.*, p. 11.

were now considered special forms of the dictatorship of the proletariat and consequently, socialist-type states. Despite the differences between the Soviet and satellite forms of state, they were only minor and would gradually disappear, leaving in its stead a completely Sovietized People's Democratic Republic.

*The Purge of the Communists.* Parallel developments in the political sphere matched the theoretical development. The revolution began to devour its children. With all the parties under the wing of the Communists, the Communists turned to a purge of its own ranks. The Tito affair caused an explosion in every satellite country. During the first few years of the satellites' existence, the Soviet Union's main aim had been to assist the local Communists in taking over the instruments of power. Loyalty, or more accurately, complete subservience to the Soviet Union had not been a criterion. The object was to attain power in every way possible. The local Communists had been left for the most part to their own devices, with only timely assistance from the Soviet Union when it had become necessary. Now the line had changed. The Tito affair had come at a time when the East-West relations were at a critical stage, when the least upheaval in the Soviet power machine might have meant a loss of initiative. The Tito affair had caused a crisis within the Cominform. Complete subservience to Moscow was now the order of the day, and those who in their duty had been too ardent in the moderate days, or those who in any way gave the least sign of independence of thought or of too much popularity and power in their own little domain, were soon to become victims of the Tito aftermath.

The first victim of the purge was Patrascanu of Rumania. The Pole, Gomulka, was soon to follow. Then came a series of show trials, Xoxe in Albania, Kostov in Bulgaria, and Rajk in Hungary. Czechoslovakia was late in its purges; Novey, Clementis, and Sling were among others purged in 1951. The Czech purge culminated in the arrest and final show trial of Slansky in 1952. The purge of the Rumanians, Luca, Georgescu and Pauker finished the procedure.

In the meantime, Yugoslavia had had its purge, conducted from another point of view. In May, 1948, in seeming anticipation of the Cominform resolution, the Minister of Light Indus-



try, Hebrang, and the Minister of Finance, Zujovic, were relieved of their duties and later arrested. Following the Cominform resolution a shakeup occurred throughout the governments of the Yugoslav constituent states, with the most severe purging in Bosnia and Montenegro. Colonel-General Jovanovic, former Chief of Staff, was shot by frontier guards while trying to escape into Rumania and other officers were captured.

The purges seemed to follow a definite pattern. The original charges against these men were only on the basis of nationalist and rightist deviations. Gradually, as the hostility between the Cominform and Yugoslavia increased, the charges were enlarged to include espionage and conspiracy to overthrow the government with the aid of Titoists, American agents, Fascists and Trotskyites. Finally, the charges of Zionism and cosmopolitanism were used, especially in the Rajk and Slansky trials. The move against the Jewish leaders in Hungary was a final touch. On the face of it, the charges of nationalism and cosmopolitanism seemed mutually exclusive. But each recognized a loyalty other than to the Soviet Union: the first to the nation, the second to an international culture. Only true proletarian internationalism was to be allowed from now on.

*The Sovietization of Society.* Concurrently with the purges, the Communists undertook a complete membership verification of their rank and file. The Party evaluated its social composition. All members were examined on the basis of their class background.

In most cases the verification was carried out in a methodical way, by examining in turn: (1) the organizers and leaders, (2) the political and technical personnel, (3) the middle party functionaries, (4) branch officials, party group active leaders, and (5) the rank and file.<sup>102</sup> The number of party members purged by this verification drive varied slightly from country to country, but a typical example was that of Rumania where nearly 192,000 members or almost 20 per cent of the membership was expelled.<sup>103</sup>

A further move toward uniformity and communist control

<sup>102</sup> Kovacs, I. "Some Results of Membership Verification in the Hungarian Workers' Party," *For a Lasting Peace, For a People's Democracy*, 4(31), February 15, 1949, p. 4.

<sup>103</sup> Gheorghiu-Dej, G. "For Purity of Party Ranks," *For a Lasting Peace, For a People's Democracy*, 25(85), June 23, 1950, p. 4.



was the reorganization of all the National Fronts into disciplined organizations with the Communists in true control. In order to come closer to the communist ideal of a Soviet-type state, the local People's Councils or Committees were reorganized during 1948-1950, and based upon the communist practice of democratic-centralism.<sup>104</sup>

In the rest of society, the move toward uniformity and sovietization was reflected in the all-out drive for collectivization, slowly at first, but then with an increasing intensity of the "class struggle." Machine-tractor stations were organized to serve as political overseers. In industry, the Soviet techniques of socialist competition or emulation with its full panoply of Stakhanovite shock workers, the movement toward piece rates and increased labor discipline were also inaugurated. Finally, the satellites undertook transformation in the cultural sphere. The drive was hailed as the beginning of a new day: "In the struggle for Socialism, in the People's Democracies, a new man is being born, a man of new morals. . . ."<sup>105</sup> The drive toward the slavish patterning of the satellite society after the model of the Soviet Union was well underway.

A discussion of the consequent events, the relative success or failure of the drive, as well as the changes that have occurred since Stalin's death are beyond the scope of this paper. The beginning of the third stage of totalitarian development with its purges and trials of the Communists, its reorganization of the Front and local committees, its collectivization, increased industrialization and cultural revolution marked the end of the last vestiges of independence for the Eastern European states.

#### A THEORY OF TOTALITARIAN DEVELOPMENT

It has been seen that the totalitarian development of Eastern Europe took place in three stages. During the first stage, the totalitarian movement existed in a non-totalitarian environment. In the second stage, the totalitarian movement patterned the state in its own image. Finally, the movement

<sup>104</sup> Mankovsky, B. S., "A New Stage in the Development of People's Democratic States as States of the Socialist Type," translated from *Sovetskoe Gosudarstvo i Pravo*, 7, 1950, 1-13, in *Current Digest of the Soviet Press*, 11:35, 1950, p. 4.

<sup>105</sup> *For a Lasting Peace, For a People's Democracy*, "Cultural Revolutions in the People's Democracies," 2(62), January 13, 1950, p. 1.

penetrated to the basic social units in the third stage. Each stage was characterized by particular attitudes and actions on the part of the Soviet Union: the first by moderation, the second by a tightening-up, and the third by a movement toward uniformity.

Corresponding to each stage of development was a rationalization for communist action in the form of a Theory of People's Democracy. Theoreticians during the first stage maintained that People's Democracy was a unique form of democracy, neither proletarian nor bourgeois, which was proceeding along an independent path of socialist development. During the second stage, the theory of an independent road to socialism was significantly toned down and the Soviet Union was hailed as the great model for building socialism. Finally in the third stage, all thought of independent development toward socialism was forgotten. Only with the help of the Soviet Union could socialism be built. The People's Democracies were now hailed as socialist-type states and particular forms of the dictatorship of the proletariat.

Each stage of totalitarian development had its specific political characteristics. During the first stage, the Communists, united with the other parties, turned against the old ruling classes and fascist collaborators. Then the Communist Party concentrated on casting the major parties contending for power out of the coalition. During the second stage, the Communists turned toward the tasks of destroying the opposition and purging every dissident element from the communist-controlled coalitions. In the third stage, the revolution began to devour its children. Communist leaders and rank and file members were purged and the drive for complete sovietization of the countries was undertaken.

There were clearly discernible techniques of power consolidation during each stage. In the first stage, the first task was to gain control of the major instruments of power: the resistance movements, trade unions, voluntary associations, the armed forces, major government ministries, and the instruments of land reform and nationalization. The next task was to turn against the opposition by means of Soviet interference, Soviet intervention, infiltration and party-splitting, duplication of parties, actions provoking resignations, intimidat-

tion and persecution, rigged elections and the compromising of the opposition. In the second stage, the opposition was destroyed by either fleeing the country or being arrested and brought to trial. The opposition parties were either dissolved or thoroughly communized. The Communists then turned against the coalition parties—the liberal and bourgeois parties, the peasant parties and the social democratic parties—each in its turn. These parties were either dissolved or purged of their right wings. Two or more parties representing the same class were merged into a united party. In the final stage, various communist leaders themselves were purged and brought to trial on charges of nationalism, cosmopolitanism, espionage and/or conspiracy. The Communists then turned toward a complete sovietization of the social, political, economic and cultural realms of life.

Finally, the dramatic impact of international events played a major role in the development of each stage of totalitarianism. What telescoping of power consolidation occurred was primarily due to the events on the international scene. The events in the first stage of moderation were influenced to a great extent by the attempt to maintain the war-time Grand Alliance of West and East for as long as politically practical. The second stage was coincident with the Marshall Plan and the consequent organization of the Cominform. The Tito affair hastened the entry into the third stage of development.

It was pointed out that in addition to the specific conditions in each country, the major advantage of the Communists in their drive for power consolidation was the physical presence of the Soviet Union and its close proximity to the Eastern European countries, while a major obstacle was the fear of Western interference and intervention. Inevitably then the question arises of whether this tragedy of Eastern Europe could have been prevented. Had the West insisted that the post-war governments of Poland and Yugoslavia be truly representative and backed up this insistence by the threat of intervention, would the Communists have refrained from finally gaining power? Could the revolution have been prevented if the United States and Great Britain had intervened with more than feeble protests when the Maniu National

Peasants and the Bratianu Liberals in Rumania and the Petkov Agrarians and the Lulchev Social Democrats in Bulgaria were cast out of the government and coalition? Possibly yes. The failure of the West to act virtually presented a *carte-blanche* to the Communists. When the West finally did act with the Marshall Plan and later with the Atlantic Pact, it was already too late to save Eastern Europe. The Western actions merely hastened the Communists on their path toward final victory. Speculation on whether the tragedy could have been avoided, however, becomes irrelevant, at least to the countries involved. History, unfortunately, knows no "ifs." The least one may hope for is that the lessons of Eastern Europe be learned quickly before similar tragedy takes its toll elsewhere.

## "MIDWAY"

### LESSONS OF MILITARY POLICY FROM A BATTLE NARRATIVE

*W. Barton Leach*

This paper is a book analysis of *Midway* (U. S. Naval Institute, 1955) by two Japanese officers, Mitsuo Fuchida and Masatake Okumiya, who were participants in the battle. My purpose is to draw lessons of policy and administration from this crushing defeat inflicted upon Japan. Page references to the book appear in the text.

#### WHY THIS TYPE OF BOOK ANALYSIS?

CIVILIAN university studies in defense policy and administration, military history, civil-military relationships and the like face a problem in regard to available published material. There is much relevant literature and documentation covering a recent global war, an even more recent limited war, an interim period of prodigal disarmament, a current period of "long haul" rearmament, and earlier episodes stretching back through the life of the Republic. Little of this has addressed itself directly to analysis of military policy; yet almost none is wholly irrelevant.

The mass of this material is formidable and its content diverse. It includes, in addition to the memoirs and histories, massive congressional and parliamentary documents. In due time the normal scholarly processes will doubtless bring this material under control for practical use. But at present a survey and initial processing may be justified.

The present analysis represents one method by which the contents of a book can be made more readily available to students of military policy and administration. The analysis is more than a review but less than a complete precis. It is a selection for one purpose of materials from a book designed for a different purpose.

The distillate we seek is the enlightenment of experience on significant issues of policy and administration, generally excluding tactics and personal narrative. I for one do not know where policy ends and administration begins. Nor do I care.<sup>1</sup>

<sup>1</sup> But this I know: any program conceived by those who think of themselves as policy makers in the Pentagon can be destroyed by the officials into whose hands it is entrusted for implementation. Maybe we need a new word. *Polistrat*, perhaps? Better still, *admi**pol**istrat*ion—not only to get in more syllables but

What matters for our purpose in a civilian university is whether the issue is, in the United States, within the purview of civilian authority. At least one episode from the book here under examination suggests that the boundaries of potential civilian influence are vague. At Midway Admiral Nagumo's delay in attacking the American carriers, as he vacillated in rearming his torpedo bombers, may have been a decisive factor (p. 237). This is a tactical decision outside the civilian sphere. Yet the choice of Nagumo, not an airman, at his age and with his characteristics (pp. 116-118) may have foreordained the vacillation. (See for contrast Churchill's reconstitution of the Middle East high command after the loss of Tobruk and before Alamein, at about this same period of the war.<sup>2</sup>)

At Midway all of the following matters, clearly within the civilian scope, seriously affected the battle:

- (a) The overemphasis on combat, at the expense of reconnaissance, in equipment, training, and standard operating procedures.
- (b) The delay in following up an early Japanese breakthrough in radar (the Yagi antenna) and, when early warning sets belatedly became available, the decision to install the first two in battleships rather than carriers.
- (c) The peacetime limitation on number and flight training of replacement crews, thus causing an available, potentially decisive, fleet carrier to be absent from the battle.
- (d) The emotional reaction to the Doolittle raid, resulting in choice of the dubious Midway operation as against strategic alternatives.
- (e) The location of Admiral Yamamoto in a radio-silenced battleship rather than ashore with fully usable radio facilities as was his adversary Nimitz.
- (f) The antipathetic rivalry between Army and Navy planners and even between Naval General Staff and Combined Fleet Headquarters.

to signify that policy is hemmed in by administration on all sides. Or, if one feels in his folly that exactly the opposite is true, *poladminicy*. After all, if Defense Studies is to qualify as a legitimate member of the social and political sciences, it should develop a jargon, the more polysyllabic the better.

For the authoritative account of the Battle of Midway see Morison, *History of U. S. Naval Operations in World War II*, vol. iv, pp. 69 ff.

<sup>2</sup> Churchill, *The Hinge of Fate*, pp. 460-462.

- (g) The euphoria induced by early victories, resulting in decisions to extend the Japanese perimeter far beyond original plans, rather than to consolidate existing conquests.

All of these, whether policy or administration, offer instruction by vicarious trial-and-error to American civilians who, from the President down, may be called upon to face problems of a similar nature. The fact that in the Japanese system these matters appear to have been decided entirely in military conclaves with no civilian participation may be the most enlightening fact of all. For the mistakes were critical and, at least by hindsight, avoidable.

One might think that the narrative of a 1942 naval defeat by two Japanese officers would offer little instruction to civilian policy makers in the United States thirteen years later. But this is not so. The battle really is the payoff. It is on the battlefield—land, sea or air—that the merits or defects of peacetime policy demonstrate themselves by triumph or disaster.

#### THE BATTLE OF MIDWAY IN ITS SETTING

This volume is an account of the Battle of Midway, June 4-6, 1942, from the Japanese side. One of the authors is an airman who, having led the attack on Pearl Harbor, was at Midway on board *Akagi*, flagship of the Carrier Striking Force. The other was a staff officer in a light force carrier. The book as originally written has been extensively revised for publication by the U. S. Naval Institute in the light of available American documentation and such authoritative works as Volume IV of Morison's *History of U. S. Naval Operations in World War II*.

Chronologically the narrative begins with the Japanese attempt in May 1942 to capture Port Moresby in Southeast New Guinea and Tulagi in the Solomons. This precipitated the carrier duel known as the Battle of the Coral Sea, which becomes relevant to the later Midway action by virtue of the changes it wrought in U. S./Japanese carrier strength. *Lexington* was lost at the Coral Sea. *Yorktown* was damaged, but was quickly restored to operational status by strenuous efforts at Pearl Harbor. *Shokaku* was damaged and was not restored to action before Midway. *Zuikaku* was undamaged but had lost so many of its flying personnel that it was not ready to sortie



with the Midway attack force. Thus the Battle of the Coral Sea, the divergent capabilities of Japanese/U. S. repair crews, and the lack of trained flying personnel to reman one undamaged Japanese fleet carrier produced a significant alteration in the balance of forces available at Midway. The effect of this change was heightened by the Japanese belief that *Yorktown* as well as *Lexington* had been sunk.

After the Coral Sea operation a strategic choice lay before the Japanese high command. Naval General Staff proposed continued actions in the South Pacific against New Calendonia, Fiji and Samoa to cut communications between the U. S. and Australia. Combined Fleet Headquarters (Admiral Yamamoto) proposed a diversionary attack on the Western Aleutians followed by capture of Midway in the expectation that the U. S. fleet would be drawn into decisive battle to dislodge the Midway occupation force and protect its main base at Pearl Harbor. Serious objections to the Midway operation were silenced by the Doolittle Tokyo raid of April 18, 1942, for the attack on Midway then assumed the aspect of an extended patrol line eastward to prevent further desecration of the Japanese home islands.

Admiral Nimitz at Pearl Harbor, correctly analyzing Japanese attack plans with the aid of *Magic* intelligence, disposed various forces to meet the attack—chiefly Task Forces 16 and 17 formed around CVs *Lexington*, *Hornet*, and *Yorktown* under Admirals Fletcher and Spruance.

The Japanese fleet, under Yamamoto's over-all command, comprised a Carrier Striking Force of four CVs (Nagumo), a Main Body of battleships with screening ships (Yamamoto), and an Invasion Force of escorted transports. It was the double mission of the Nagumo Carrier Striking Force to neutralize Midway by air attack and to engage U. S. carriers when they should appear. The Japanese forces were detected and shadowed; the U. S. task forces were not. After Nagumo threw one strike at Midway, Spruance attacked his carriers at their most vulnerable moment—when refueling and rearming their aircraft. The results of a complex naval action were:

- (a) The Japanese lost all four of their participating fleet carriers. The U.S. lost one, *Yorktown*. Thus was rectified the serious

adverse imbalance of naval air in the Pacific. The future turned on the competition of the ship yards in which the Japanese never had a chance.

- (b) The attack on Midway failed. This was the turning of the tide. The course of the war showed no further expansion of Japanese-controlled territory, only a contraction until zero was reached.

In a chapter entitled "Analysis of the Defeat" the authors provide a tactical critique useful chiefly to military professionals; but in this chapter and elsewhere they also offer precepts of value to a broader audience.

#### INTELLIGENCE AT MIDWAY, WITH A LONG GLANCE AT TRAINING AND R & D

In the poker game of the Pacific the code-breaking exploit known as *Magic* gave Nimitz a mirror behind the back of his opponent. But unlike poker, war is a game where a player cannot throw in his hand; and Nimitz's opponent held the stronger cards and the initiative to raise the bets. Even after *Magic* had dictated the mobilization of Nimitz's whole force of fleet carriers for Midway, Yamamoto outnumbered him in CVs 5 to 3, to say nothing of several available CVLs and a fleet of battleships and cruisers. *Magic* could be little help to Nimitz in this circumstance, but other intelligence factors intervened.

First, it was assumed that tactical surprise would be achieved and that the Nagumo carrier force would perform its dual mission of Midway attack and fleet battle in sequence, not simultaneously. An intelligence failure caused Naval General Staff to report to Yamamoto on June 1 that an American carrier force was operating in the South Pacific (p. 133), a fact which in conjunction with Yamamoto's knowledge of Nimitz's order of battle eliminated any chance of an early carrier encounter around Midway. This absence of American carriers from the central Pacific had been so confidently expected that one of Yamamoto's fleet carriers and one light carrier were detached to accompany the diversionary attack upon the Aleutians (p. 257). Furthermore, no plan was prepared for the situation that occurred—an attack upon the Nagumo force while it was striking Midway (pp. 97, 134). Junior officers

considered this unsatisfactory but dared not speak up (p. 99). No prodding mind in superior authority asked the hard questions to assure that confidence and audacity were backed with solid planning against contingencies—as, for instance, Churchill prodded Auchinleck during Rommel's offensive taking place at the same moment.<sup>3</sup>

Second, the Japanese fleet suffered from repeated reconnaissance failures, resulting in failure to locate the Fletcher-Spruance carriers. The fleet contained no organic reconnaissance units of any size; it had no carrier-borne planes designed especially for search; and pilots got training in reconnaissance only as part of their original general curriculum with no subsequent special training (pp. 148, 149). These deficiencies of training and equipment were failures of peacetime policy.

Third, the peacetime Research and Development effort had been inadequate to provide the two types of radar relevant to carrier actions—early warning to spot attacking aircraft at a distance in all weather round the clock, and air-to-surface-vessel (ASV) to permit reconnaissance planes to locate enemy carriers regardless of visibility (pp. 147, 245, 144). The U. S. fleet, having both types,<sup>4</sup> had an incomparable advantage in tactical intelligence. The book does not, of course, identify the individual who made the peacetime decision that withheld funds or scientific personnel from this vital R & D effort, but he bears a heavy burden of responsibility to his countrymen. There obviously was no such civilian pressure behind this development as Sir Robert Watson-Watt enjoyed from the Air Defense Research Technical Subcommittee<sup>5</sup> as he developed Britain's radar defenses in the 1930's. In despairing comments the authors note that a critical radar component, the "Yagi antenna," was invented by a Japanese in 1932, put to use by Britain and the United States, and neglected by the Japanese; and the only two early warning sets in the Yamamoto fleet, "bread board" models at that, were installed in battleships 300 miles away from the carriers (pp. 243–244).

<sup>3</sup> Churchill to Auchinleck and Tedder, 2 June 1942, quoted in Churchill, *The Hinge of Fate*, p. 361.

<sup>4</sup> U. S. forces had early warning radar at Midway and on the three CVs. Some Midway-based planes had ASV, but apparently the carrier-based planes did not. Morison, *U. S. Naval Operations in World War II*, vol. iv, pp. 83, 96–99.

<sup>5</sup> Churchill, *The Gathering Storm*, p. 154.

FAKING THE WAR GAMES

The prostitution of staff work is no Japanese invention, but it is rarely brought out in the open with full clarity as in this volume. There are many devices for such prostitution, all having as a common element the Dictated Solution. It is the purpose of staff work to reach a solution based upon fact and logic; it is a prostitution of staff work when the solution is reached in advance and the staff is then put to work to support it, falsifying facts or distorting logic if necessary. One method is to doctor the intelligence as to enemy forces and capabilities—to sneer at intelligence estimates as academic or even venally inspired—to say in substance, when all else fails, "I just don't believe they're that good." Another method is to exaggerate one's own capabilities—bombing accuracy, for instance. Another is to juggle the results of a war game designed to test the soundness of an operational plan. This is what Yamamoto's Chief of Staff did before Midway as described by the authors (p. 96):

In the tabletop maneuvers a situation developed in which the Nagumo Force underwent a bombing attack by enemy land-based aircraft while its own planes were off attacking Midway. In accordance with the rules [the Umpire] ruled that there had been nine enemy hits on the Japanese carriers. Both *Akagi* and *Kaga* were listed as sunk. Admiral Ugaki, however, arbitrarily reduced the number of enemy hits to only three, which resulted in *Kaga's* still being ruled sunk but *Akagi* only slightly damaged. . . . Even this revised ruling was subsequently cancelled, and *Kaga* reappeared as a participant in the next part of the games covering the New Caledonia and Fiji Islands invasions. The verdicts of the umpires regarding the results of air fighting were similarly juggled, always in favor of the Japanese forces.

That such things can happen—and produce such disasters—is a caution to any leader, in or out of uniform.

THE IMPULSIVE RESPONSE TO A THREAT TO THE HOMELAND

Serious, reasoned objections to Yamamoto's Midway Plan were advanced by the Naval General Staff in early April (pp. 57–59). Upon Yamamoto's insistence on the plan General Staff gave only a tentative assent in principle (p. 63). Then

the Doolittle raid, demonstrating a possibility that the homeland would be subjected to further attack, stilled the Staff objections and led to the adoption of the disastrous Midway plan as a means of stopping further raids (pp. 64-72). It is perhaps significant that the issue seems to have been settled between Naval Staff and Combined Fleet without reference to higher authority.<sup>6</sup> Certainly, in the Anglo-American democracies, such a major shift of strategic direction would be passed upon at the political level. Under these circumstances the emotional reaction to an attack of trifling weight, though great morale effect on both sides, might have been dampened. Probably only a political authority can take such decisions as Churchill's in exposing the British homeland to threatened invasion by sending crucial armored forces to support the battle in the African desert.<sup>7</sup> In the event of atomic war agonizing choices may have to be made as between defense of homeland cities, forces in the field, or counter-attack air bases.

*Yorktown and Shokaku*—WHAT HAPPENS WHEN "SUPPORT FORCES" ARE DEPLETED

There is a tendency, especially in peacetime, to assume that the only elements of military power that really count are those that fight—the men behind the guns, with the ships, or in the air. There is a tendency to point with pride at increases in the percentage of men in combat units and to elimination of "supporting units," as if the latter were frills. Lord Ismay has warned against the "division counters" in his *NATO, The First Five Years* (p. 101), and has emphasized the need for supporting units to permit *sustained* operations. *Yorktown* and *Shokaku* provide a case in point. Both were damaged at the Coral Sea. *Yorktown*, "with damage calculated to take three months to repair"<sup>8</sup> was made battleworthy in 48 hours by the repair crews at Pearl Harbor. *Shokaku*, apparently damaged to about the same degree, was accorded "lackadaisical effort" and failed to make the battle (p. 107). Thus the balance of CVs at Midway was 4 to 3, instead of 5 to 3 (if *Shokaku* had

<sup>6</sup> Imperial Headquarters obliged with a terse order (Morison, *op. cit.* vol. iv, p. 75) but this appears to have been a formality representing no real participation.

<sup>7</sup> Churchill, *Their Finest Hour*, p. 430.

<sup>8</sup> Churchill, *The Hinge of Fate*, p. 249; Morison, *op. cit.* vol. iv, p. 81.

received similar treatment from support forces) or 4 to 2 (if the Pearl Harbor crews had been equally lackadaisical).

*Yorktown* AND *Zuikaku*—WHAT HAPPENS WHEN REPLACEMENT CREWS OR FLYING HOURS ARE CUT

Not only was *Yorktown* badly damaged at the Coral Sea. Her aircraft and air crews were in need of relief; and undamaged *Zuikaku* was in similar circumstance. But *Yorktown* made the Battle of Midway, and *Zuikaku* did not. A new air group was ready to board *Yorktown*<sup>9</sup> but not *Zuikaku* (pp. 106, 243). This pattern persisted throughout the war; as the fighting progressed the limiting factor on Japanese air power was not aircraft but crews.<sup>10</sup> They never caught up with the training deficiencies of the early days and hence suffered the 20-to-1 loss ratios of the 1944 "turkey shoots." The JAF had the false front of a Potemkin village due to its lack of depth in crews per aircraft at the outset. In peacetime it is a constant temptation to reduce the number of crews per aircraft—a risky business. And, when economy is dictated from fiscal sources, an apparently easy way to achieve "savings" is to reduce flying hours and save Maintenance and Operations funds at the expense of crew efficiency. At Midway these policies prevented a further, possibly decisive, weighting of the scales in favor of Japan. Of course *Shokaku*, too, would have been immobilized by lack of trained air crews even if she had been promptly repaired.

COMMAND PERSONALITIES; THE JAPANESE OFFICER CORPS

Two comments on key individual commanders and two on the Japanese officer corps are enlightening.

Of the individuals Yamamoto was for *l'attaque, toujours l'attaque*, even to the point of allowing alteration of the results of a war game to justify an over-extended offensive operation. He, with some help from the Naval General Staff, put the rosiest possible interpretation on all intelligence as to American forces and deployment. He suffered from an acute case of "the inherent Japanese tendency toward wishful thinking" (p. 130). From Combined Fleet Headquarters he dominated the Naval General Staff on issues within the authority of the latter

<sup>9</sup> *Ibid.*

<sup>10</sup> *U. S. Strategic Bombing Survey, Summary Report (Pacific War)*, p. 9 (1946).



(p. 61). The conflict between General MacArthur and Washington during the Korean War immediately comes to mind as a parallel, though the outcome was different. In American experience there have been instances where field commanders had practical authority at Departmental level similar to that enjoyed by Yamamoto—and were permitted to have such authority by the responsible civilians.

Nagumo, a vigorously imaginative officer in earlier years (p. 117), had become less decisive with age. As seniority placed him in command of types of forces with which he had never served in lower grades he progressively abdicated authority to his staff (pp. 117–118). Then, when faced with crucial decisions of tactics and timing at Midway—decisions he could not delegate—he temporized and lost any chance to extricate his force (p. 237).

As to the Japanese naval officer corps generally, the authors declare it reflected a preference for affability over troublesome tendencies to challenge traditional concepts, assert independent ideas, and advocate new weapons and tactics, especially those of the air (p. 75). Further, they say, the younger officers were unduly subservient to higher authority. They grumbled among themselves at the Midway plan, especially the rigging of the war game, but thought it prudent to say nothing to their superiors (p. 99). These are symptoms of a force destined to defeat, unless of course the opposing force suffers from similar defects.

#### CIVILIAN CONTROL JAPANESE-STYLE

This book of 260 pages contains only one reference to the Navy Minister or any other political authority. The reference is a quotation from the diary of Admiral Ugaki, he who faked the war game:

Fukudome [Chief First Section, Naval General Staff] told me that he had postponed the decision advocated by [Navy Minister] Shimada<sup>11</sup> to halt construction of *Musashi*. It is generally considered

<sup>11</sup> In accordance with Japanese practice Shimada was not a civilian but an admiral. He was Commander-in-Chief of the Japanese fleet in China in 1940, then became Navy Minister in 1941. Tried as a war criminal in 1945, he was sentenced to life imprisonment.



that the battleship is a worthy instrument of service, and until there are other means of nullifying the enemy's battleships, our own battleship strength must be maintained. (p. 242)

*Musashi* was the second of the enormous 18-inch-gun battleships of which *Yamato* was the first. The use of limited steel and skilled manpower for these outdated instruments of war was the despair of many officers (p. 240). They never saw significant service. But under the Japanese system the "decision advocated" by the Navy Minister was "postponed," i.e. rejected, by the Naval General Staff.

The relationship between civilian and professional authority in a military establishment is a matter of great subtlety. Its characteristics should be selflessness, deserved mutual respect, and shared singlemindedness in serving the national purpose. In some of its most useful manifestations the civilian authority can resist the pull of seniority in personnel selection (Nagumo, perhaps) and of tradition in strategic concepts (the *Musashi*). It can also assure that shoddy expedients such as the faking of war games<sup>12</sup> are exposed or never attempted. The authors of the book cry out against the commitment of huge resources to construction of super-battleships (p. 240), the concept that the longed-for fleet engagement would be a battleship duel with carriers in a supporting role (p. 47), the failure to provide adequate numbers of air crews (p. 242), the lack of sufficient drive behind the development of radar (p. 244), the Victory Disease of overconfidence induced by early success (p. 245)—all without any apparent realization that the sobering necessity of justifying such things to a knowledgeable, insistent civilian authority might have produced a different result.

<sup>12</sup> Such a scandalous and disastrous business could never have survived the pre-OVERLORD war game and briefing provided by General (now Field Marshal) Montgomery at St. Paul's School for the SHAEF staff, the King, Churchill, Smuts and others. See Kingston-McCloughry, *The Direction of War*, pp. 134-135.

As this analysis is being written a related instance of Japanese intra-mural deception has appeared. The publication of the Yoshida Memoirs discloses that the Japanese decision to go to war was induced, in part at least, by the war party doctoring Cordell Hull's message of 26 November 1941 so that it appeared to be an ultimatum. (Arthur Krock in *N. Y. Times*, 9 September 1955.) Can such things happen here? An article in *Time*, 3 November 1952, asserts that the withdrawal of U. S. troops from Korea in 1949, unquestionably a major cause of the attack on the ROK in 1950, was produced in part by a doctoring of a message from General MacArthur in a National Security Council document.

## CONCLUSION

The reader will not have failed to note that some of the Japanese mistakes before Midway—mistakes that predetermined the outcome of the battle—may be in process or in contemplation elsewhere at the present writing (September, 1955). Surely one of the uses of history is to let others make our mistakes for us. We are wise if we can obtain benefits approaching those of personal experience while suffering only vicarious defeats.

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